THE DEVELOPMENT OF UNIFORM INTERNATIONAL ACCOUNTING: AN ENQUIRY INTO THE PROBLEMS, PROGRESS AND PROSPECTS

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THESIS

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December 1975

Thesis Advisor: J. M. Fremgen

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This study has evolved from a scrutiny of the growing wealth of literature that concerns itself with the problems of international accounting. This study leads to a conclusion supporting the development of uniform international accounting.

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An Enquiry into the Problems, Progress and Prospects

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B.S., Pakistan Naval Academy, 1972

Submitted in partial fulfillment of the
requirements for the degree of

MASTER OF SCIENCE IN MANAGEMENT

from the

NAVAL POSTGRADUATE SCHOOL

December 1975

ABSTRACT

The last three decades have witnessed a rapidly growing internationalization of business activities. Because the accounting standards and practices of different countries have developed in response to diverse environments, accounting has developed with strong national accents. Consequently, an enterprise with investments in many countries has difficulty in achieving a consolidated financial report from a multiplicity of accounting practices. Further, the investors in these enterprises find it difficult to understand and evaluate the financial statements developed from a wide range of accounting standards.

The accounting profession has addressed itself to these problems at recent international congresses of accountants. It established the International Coordination Committee for the Accounting Profession and the International Accounting Standards Committee with the specific objective of developing uniform international accounting standards.

This study has evolved from a scrutiny of the growing wealth of literature that concerns itself with the problems of international accounting. This study leads to a conclusion supporting the development of uniform international accounting.

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"We are born for cooperation," wrote the Roman Emperor Marcus Aurelius more than 2000 years ago. While this may or may not have been the ideal of professions and trades over the ages, it would seem that human nature has another facet that tends to contradict and nullify this noble concept.

Robert Ardrey, in his classic work, The Territorial Imperative, makes clear that all animals--including human animals--have a powerful instinct to defend their own territory. Birds, beasts, and people naturally resist invasion. They do not take into consideration whether or not the invasion may be of benefit to them, and they instinctively resist it. Moreover, unless the odds against them are overwhelming, the defenders usually win.

In the case of accountants, it is not a geographical territory that they are primarily interested in defending; it is the field of accounting practice to which they lay claim. It is this territory which accountants the world over regard as their own special domain and which they would preserve from the incursions of other accountants. Whether accountants have the mental training that evolves from functioning in a centralized control system under socialism or communism or in a free enterprise with a minimum of government control, they create instinctive barriers against all outside invasions. Whether it is called national pride or the political expediency of nationalism, the conscious or subconscious conception always seems to be: "My country, right or wrong."

It would seem, though, that Marcus Aurelius was not far wrong and that, in our shrinking world of rapid communications and growing interdependency, the very survival of all civilized institutions may ultimately come to depend on cooperation. The accountant and his profession are no exception to this inevitable development, and both are having to realize that international business and investment activities have placed a new burden of cooperation upon them.

In an editorial written twelve years ago, The Canadian Chartered Accountant was early in giving succinct expression to this new responsibility confronting the accounting professions of all countries:

> In a world economy that is becoming closer knit, and with the growing international character of business and the desirability of investment in the underdeveloped countries, there is a need for a reliable means of international financial communication. To the extent that accounting principles, as commonly applied, differ from country to country, so financial statements prepared according to local concepts will fail to convey the proper message to the overseas investor. Probably even more crucial is the need for common high professional standards in auditing practice so that the investor will be able to place the same reliance on certified statements whatever the country of origin.

Even the attainment of this latter objective may not be adequate to the demands of the present day. Professor Gerhard Mueller maintains that it is not enough to produce highly reliable financial statements that are attested to by qualified independent auditors if the statements are not comprehensively meaningful to readers in other countries, should circumstances require the use of the information across international borders. He draws attention to the dilemma of different national accounting

practices which have evolved in distinctly separate accounting environments and to the resultant obstacles in the way of universally meaningful financial reporting. [2:235].

A growing flow of periodical literature dealing with the increasing needs of international communication in a common accounting language is evidently having the effect of eroding the traditional regard for the notion that financial reporting falls mainly into national domains. An international dimension of financial reporting is being increasingly recognized. The now substantial volume of literature on international accounting conveys both an urgency and a broad outlook that are rather new in discussions of accounting matters. [2:123].

However, it may reasonably be assumed that, as long as accounting standards vary from country to country, complete international understanding in the field of accounting must remain unattainable. In the present state of the art there are problems that must be resolved. Accounting standards, whether national or international, govern the contents of published financial statements. The contents of such statements will vary widely, depending upon the standards or lack of standards in force. The development of a rational set of accounting standards requires an identification of the various classes of users of financial statements and a clear conception of the information needs of each class of user. These needs are bound to vary considerably among countries as diverse as Russia, China, the nations of South America, India, Saudi Arabia, Nigeria, and the nations of Western Europe and

North America. The legal, economic, political, social and cultural conditions in these areas vary so widely from one to the other that the possibility of a universal or international system of accounting principles adopted by all countries is going to present accounting professions throughout the world with a challenge of unprecedented magnitude. This challenge must make the accountant aware that there are different principles from those used in his own country. He must become multiple-principle conscious. This would give him a deeper understanding of the relationships and effects of one country's principles and practices as compared and contrasted with those of another country. He must become concerned with the effect of these relationships on the accounting systems of the various countries. [3:2, 4:64-67]. The burden of this challenge falls heaviest on the shoulders of accountants of those countries whose development of accounting principles and practices have achieved the most advanced stages of maturity--the United States, Britain and Canada.

The problems that constitute this new challenge to the accounting professions of all countries must be considered in depth if there is to be even a marginal possibility of coming to grips with it. It is therefore proposed to identify some of these problems in this chapter. These problems may be primarily responsible for the existing diversity in accounting principles and practices among the community of nations. The extent of this diversity will be treated in Chapter III, which will serve to reinforce the magnitude of the problems identified in the paragraphs that follow.

A. LEGAL CONSTRAINTS

One significant problem is the variety of legal constraints and conditions which are found in different countries. The legal requirements determine the form and content of financial statements and the standards of disclosure which are expected within the jurisdiction. In many cases legal requirements also dictate rules of income and value determination. For example, depreciation methods and inventory valuation practices have been influenced considerably in the United States by tax considerations. The Securities and Exchange Commission has also exerted considerable influence on both of these accounting practices.

The legal structure of a particular country may stem from many historical sources. The Code of Hammurabi, the Mosaic Law, the Law of Islam, Roman Law, the Code of Napoleon are only a few legal structures erected by man to control his social activities. Each is based on a different philosophy springing from the unique purposes of the society for which it was devised. The impact of each legal code on business activities and accounting usages will differ with these purposes. As an example, the nations of Northern Europe have their legal institutions rooted in the Common Law, from which the United States also derives its basic legal tenets, while the Mediterranean countries owe their legal institutions basically to the Civil Code. In essence, the Common Law says, "Thou shalt not" and assumes innocence until proven otherwise. This naturally leaves wide latitude for initiative. The Civil Code's "Thou shalt"

and an assumption of guilt until proven innocent creates rigidity and a tendency to devise techniques to circumvent the Code. [5:13-16]. Is it any wonder that the inheritors of the Common Law have developed accounting professions which attained a degree of sophistication and repute which is certainly ahead of those burdened with the rigid traditions of the Civil Code?

B. RELIGIOUS TENETS

These have evidently affected business practices in various ways. The Protestant ethic of hard work for its own sake and the Protestant doctrine that the individual should be free to seek after his own welfare through work have perhaps influenced business practices in Western Europe and the United States. Nepotism, which is closely associated with the religious practices of many Eastern cultures and accepted in some Western countries as well, has probably had a significant influence on the manner of conducting business in those countries where it is prevalent. The attitudes of some religions toward usury have probably also had their impact on the nature of financial transactions. Since accounting is the language of business, it is likely that accounting practices would be influenced by variations in business practices. In this manner religious tenets, through their influence on business norms, have probably also influenced accounting practices.

C. NATIONALISM

National pride, or national vanity, often prevents us from seeing the merits of ideas and practices which have been

developed in other countries. This aspect has been mentioned in a different context at the beginning of this chapter. The accounting profession of the United States undoubtedly leads the world in the advancement of accounting concepts, principles and practices and, for just this reason, should beware of the preconceived notion that U.S. accounting principles are goals to which others should aspire and that the worldwide accounting principles which international congresses are endeavoring to develop will necessarily be identical with U.S. generally accepted accounting principles. [4:64-67].

D. COMMUNICATIONS AND THE LANGUAGE BARRIER

One of the most important means for the promotion of international communications between accountants is the academic and the professional literature. Within the English-speaking world this has provided an important means of breaking down international barriers. Unfortunately, most accountants in the English-speaking world have not been able to avail themselves of the writings of their colleagues in the remaining countries of the world. It is, of course, the language barrier which provides the main obstacle to such communications and knowledge. In the sciences this barrier has been overcome by the widespread publication of translations and abstracts of articles in foreign languages. The world of accounting, if it is to rise to the challenge of the times, will have to embark upon a similar venture. Since accounting is itself a language, an information system and a means of communication, it would be a strange irony if the problems of communications stood in the

way of the profession's increasingly important role of promoting international business.

E. BUSINESS ENVIRONMENT

The business customs and environments among countries vary widely, and these have a direct impact on accounting, the language of business. Financial reporting practices which may serve the requirements of a one-crop agrarian economy are hopelessly inadequate in a highly diversified and complex industrial economy. Even though there have been a few common strands running through the diverse fabric of world accounting systems, such as the movement of double entry bookkeeping from Italy through Central Europe to other countries, the fact remains that the middle of the twentieth century found accounting very much the preserve of individual countries and their business and economic environments. Up to this stage in the evolution of the accounting art there really had not been much of a forum for international thought and experience, because the inevitable and growing interdependence among nations had not received any appreciable recognition before the 1950s. And, when this interdependence began to manifest itself, it was only bilateral or regional in nature. Examples are the accounting interactions between Canada and the United States and within the European Common Market. [2:117-118].

During the last two decades this limited accounting communication has rapidly been transformed, and accounting information as a vehicle of international financial reporting has rapidly gained in importance.

F. NEW CHALLENGES

The foregoing factors (and there may have been others, too) which had contributed to confine accounting systems within nationalistic ivory towers, very soon became obstacles in the way of effective accounting communication.

1. Increasing International Business

The sharp increase in the need for international financial reporting has been brought about by the ever growing scale on which international business activity is conducted. For example, many U.S. corporations operate significant subsidiary companies in other countries. Also, firms incorporated outside the U.S. operate in the U.S. and third countries. It is no longer a matter of curiosity to find corporations with a majority of their total assets located in countries other than those of their respective incorporations and with more than one-half of their reported net earnings derived from sources abroad. These corporations have to rely heavily on accounting reports to manage their international business operations and to plan for future actions in the international field. Growing international investments are another factor leading to requirements for the uniformity of accounting information on an international scale to an ever greater extent. The volume of international investments reveals itself through the steadily growing amount of securities from various countries that are traded on the major stock exchanges of the world. This is not just a case of the flow of investment capital into the United States, but also of many U.S. corporations having their

securities listed on stock exchanges in other countries. Moreover, the amount of securities from other countries being traded on the major stock exchanges of the world is steadily growing. Among the U.S. corporations having formal stock listings overseas are International Business Machines, Standard Oil Company of New Jersey, International Telephone and Telegraph Company, General Motors Corporation and Ford Motor Company. [2:118].

In addition, banks all over the world are competing to finance business opportunities outside their own countries. Accounting information is essential to these investment activities, to the extent that the International Finance Corporation considered it necessary to issue a special booklet on international accounting and reporting requirements for IFC's purposes. [2:220].

2. Growing Public Demands

In an age of growing interdependence, public demands upon accounting information are increasing. The European Economic Community is the most sophisticated, but by no means the only, joint economic venture among nations of the same region; and the economic affairs of these regions have to rely on mutually acceptable and comprehensible financial reporting systems for their economic administration. [2:121-122].

The developments of the past two decades, which are in direct conflict with the factors of nationalistic prejudices, cultural background, legal constraints, etc., have inevitably given rise to many problems which have to

be resolved. The first to experience the direct impact of these problems have, of course, been the individual business units. If a company has prepared its financial reports fully in accordance with the standards and procedures of its home country, it often finds itself obligated to prepare and publish a second set of financial reports merely because it wishes to list its securities on the stock exchange of another country. This is the case for many European companies whose securities are listed on the New York Stock Exchange because they are then subject to the provisions of the Securities and Exchange Commission. It seems wasteful to have to prepare two different sets of financial statements at the same time by the same company solely because the reporting requirements of different countries are not in harmony with one another. The accounting world is faced with the problem of having to find ways to accommodate single financial reporting for international as well as national purposes, while accepting the single domicile concept of independent companies. [2:164-165].

3. International Subsidiaries

There is also the problem of the international subsidiary which has primary reporting obligations to the parent company which controls its operations. The usual practice is to require the subsidiary to adopt the same chart of accounts as the parent and also to bring its reporting format into line with that of the parent, in order to facilitate financial statement consolidation at the enterprise level. At the same time the subsidiary is required to comply with the laws of the country in which it

is chartered. This often leads to local financial reporting in compliance with local statutory requirements which are at variance with the parent company's reporting requirements. In addition, local business competition may necessitate still another type of reporting that is in line with local business customs. These conflicting reporting patterns become a serious problem for the international subsidiary. [2:164-165].

Taxation laws have earlier been mentioned as one of the significant contributing factors in the diversity of accounting practices in different countries. Taxation laws sometimes become a problem with a different dimension for foreign subsidiaries. The taxation laws of many countries, while not statutorily binding a company to a particular accounting practice, do require that certain tax accounting methods and procedures may be used only if these same methods are also employed for general financial accounting purposes. An instance of this is West Germany where, if a particular accounting treatment is to be used for tax purposes, it must also be followed in the financial accounts. If, for example, in West Germany an entity desires to obtain a tax advantage through the use of accelerated depreciation, it must be prepared to use accelerated depreciation also for financial reporting purposes. [23:30]. This of course implies a lower net income in the early years of an asset's economic life than would be the case under straight line depreciation. Other countries in which this requirement exists include France [8:216] and Lebanon [8:362, 364]. Naturally, this requirement

may result in conflicts. In a period of high tax rates the foreign subsidiary must choose between harmony with the parent's accounting procedures and more beneficial tax assessments.

4. The Growth of International and Multinational Corporations

The truly international corporation has become an important fact of life in business affairs. This fairly recent phenomenon has come about through the development of rapid communications systems, leading to a new international awareness among people in most parts of the world. The international accounting problems of this relatively recent type of business entity are significantly more encompassing than in any other area and require special attention because they are unique. Professor Gerhard Mueller has delineated the characteristics of the international corporation as follows:

> An international corporation is distinct from a national corporation with international business operations. The former has a global perspective in all of its business activities. It considers itself an international citizen. Its management is likely to consist of persons representing several nationalities and its employees are drawn from available sources all over the world. Its business organization and its planning have international horizons. The international corporation feels at home in all of the major markets of the world. It purchases its material and supplies where it can do so most economically without specific regard for national political boundaries. It manufactures products and performs services at locations where it is comparatively most feasible to do so, and its distribution systems and promotional activities are multinational in every respect. It adopts, for all of its purposes, a truly international point of view. Thus an international business attitude is a major distinguishing mark of international operations. [2:205].

Professor Mueller draws a distinct contrast between the international corporation and the national corporation

which has expanded its interests to other countries. Since this digression is useful for a deeper appreciation of the problems of international accounting to which these giants have given occasion, it would be instructive to prolong it a little further. Mueller goes on to say:

> On the other hand, the national corporation with international business activities maintains its major business orientation to a single country. Its administrative procedures reflect business philosophies and practices customary in a given national environment. This type of company strives to be known as a United States company, a British company, a Japanese company, and so on. It may be engaged in international business but it does this as an adjunct to its regular or national business. Most likely it will have an international division or several international branches, but these organizational cells have parallel status with other domestic divisions or branches. Therefore international business operates side by side with domestic business in these companies. This is clearly different from imposing an international viewpoint on all the company's business activities. [2:205].

Mueller cites the import-export trade as typical of the national corporation with international business activities, because it uses international markets to supplement given national business activities without changing the basic nature of the firm, while only enlarging the scope of the business in a certain direction.

Since there are no internationally accepted principles of accounting, the international corporation faces a dilemma with regard to the accounting practices it should employ. Business operations carried on by an international corporation in many different countries and subject to as many different legal jurisdictions cannot avoid the simultaneous observance of different accounting practices. In some instances, accounting practices may be dictated by law; in others, by locally

applicable business customs; and in still others, by professional organizations of independent accountants and auditors. From among all of these, the international corporation must somehow select a single set of accounting practices so that it can present meaningful information having some sort of common basis to its top management, its stockholders, its creditors, and to other interested parties. This is indeed a formidable problem.

We are compelled to recognize that it would be unrealistic simply to enforce the accounting practices of any single country in all the countries and situations in which the international corporation operates. For example, the arbitrary insistance on the use of United States' generally accepted accounting principles in France might produce illogical results. The French business environment is quite different from that of the United States and, therefore, is unlikely to lend itself conveniently to any attempt to express it in terms of rules and procedures appropriate to the United States. Even more revealing would be an attempt to apply United States' generally accepted accounting principles to a country like Brazil, where the pronounced inflationary tendencies would make nonsense of the strict adherence to historical cost accounting rules practiced in the United States. [2:213]. In fact, even in the United States, where inflationary problems are minor compared to Brazil, the concept of historical cost is being questioned by many accountants.

International corporations need sets of accounting practices that have an international rather than a national orientation. Moreover, until the day comes when all countries are able to adopt and implement uniform accounting practices, international corporations are unlikely to find it possible to be served by any single set of accounting practices adopted without reference to existing accounting diversities throughout the world. The different environmental conditions, business practices and legal influences are sufficiently out of alignment with each other as to make absolute accounting uniformity by any one concern rather meaningless. For the present the international corporation has no alternative but to be flexible enough to respond to the varying conditions it encounters. [2:216]. It seems, therefore, logical for the international corporation to approach the problem of selecting accounting practices suitable to its requirements from a general rather than a specific point of view and not, for example, try to force price index adjustments in countries where reliable indexes are just not available. It need hardly be added that, if the existing diversities outlined in this chapter turn out to be beyond reconciliation into an internationally uniform accounting system, then the international corporation must prepare itself to continue in this fashion perpetually into the future. However, there may be grounds for believing that such is not necessarily a foregone conclusion.

G. INFLEXIBILITIES

These, then, are the monumental problems confronting the accounting professions in a rapidly integrating system of world business and finance, and it is necessary now to take a first look at the possibilities of effectively dealing with them.

Until these problems began to emerge, the absence of accounting rules in most countries had permitted a U.S. based company to use U.S. accounting standards throughout the world or for such a company to adjust to U.S. standards without undue difficulty. But the professional pronouncements in several other countries have steadily become more strict, detailed and enforceable; and they frequently include requirements in conflict with the United States' generally accepted accounting principles as developed mainly through the bulletins, statements, opinions, recommendations and interpretations of the American Institute of Certified Public Accountants (AICPA), the Financial Accounting Standards Board (FASB), and the Securities and Exchange Commission (SEC). [8:659]. U.S. principles, in their turn, were also becoming more strict, detailed and enforceable. This was the inevitable result of countries not working toward common objectives. [6:20].

H. A BEGINNING TOWARD UNIFORMITY

Modest attempts to move in the same direction were indeed made by Canada, the United States and the United Kingdom through the Accountants International Study Group. Also, the Common Market countries have been working toward uniform accounting

standards, based largely on German practices. The United Kingdom entry into the Common Market may have the effect of moving U.K. standards away from U.S. standards and toward those of the E.E.C. [6:20].

As standards become more fixed in each country, it may become more difficult to bring about the changes needed to progress toward a single set of international standards, which the problems outlined in this chapter seem to suggest as a desirable goal. If this is so, now may be the time for the U.S. and other developed nations to join and agree on at least a broad set of international standards of accounting. A beginning has indeed been made by the formation of the International Coordination Committee for the Accounting Profession (ICCAP) at the Tenth International Congress of Accountants in Sydney, Australia, in October 1972. The functions and objectives of this organization will be described in a subsequent chapter. Suffice it to say here that the enormity of the problems may be such that any real progress in resolving them may require something more ambitious, such as the establishment of a permanent international secretariat.

II. INTERNATIONAL ACCOUNTING--A RANGE OF CONCEPTS

There is an expression in French which says: 'Pour discutur on droit etre d'accord'. This means that 'in order to be able to discuss you have to agree'. Since international accounting is increasingly becoming a challenging and rapidly developing field of study within the accounting professions of the world, it is necessary that there should be some measure of agreement as to what that term means. This is obviously a prerequisite to any attempt by the accounting professions to deal with the multifarious problems which international accounting has come to represent. This chapter attempts to reveal what some of the current literature has to say about the subject.

In Webster's dictionary the term 'international' is defined as 'affecting or involving two or more nations'. The American Accounting Association, in one of its publications [12:1], has defined accounting as 'the process of identifying, measuring, and communicating economic information to permit informed judgements and decisions by users of the information'. Perhaps, then, 'international accounting' may be taken to mean the process of identifying, measuring, and communicating economic information in some way that involves users in two or more nations.

To date, the accounting literature has not provided an explicit definition of the term 'international accounting'. Neither the International Coordination Committee for the

Accounting Profession (ICCAP) nor the International Accounting Standards Committee (IASC), although created to deal with the problems relating to international accounting, appears to have come up with a definition of it; and a uniformly accepted definition has indeed not yet been formulated. This is not to imply that the current literature is silent on the subject. On the contrary, 'international accounting' has been accorded a variety of meanings. While some authors assume international accounting to mean the body of all accounting concepts and procedures of all countries taken as a whole, others consider the term to mean the international standardization of accounting. This could mean anything from a broad set of concepts and standards that can be adopted by all countries, to the details of the system of accounting, including the method of classification of accounts (chart of accounts) and the application of uniform standards, principles, practices, and methods of reporting.

A. FANTL'S THREE CONCEPTS

Professor Irving L. Fantl [14:3-8] considers that there are three different concepts with which international accounting can be equated. It is proposed in this chapter to use these concepts as reference points. By comparing the concepts of other writers with these reference points, an attempt will be made to narrow all the differing concepts of the term 'international accounting' to three basic categories. Until a universally acceptable definition of the term 'international accounting' can be developed, it may be practicable to give a

name to each of these three concepts and to work with all of them. In other words, it may be possible to classify the discussion of each writer according to the one of the three concepts to which it is most relevant.

Professor Fantl considers that international accounting may be viewed variously as a universal system which he has named world accounting, as a descriptive approach covering all the accounting standards and practices of all countries, or as the accounting for a parent company and its foreign subsidiaries.

Within the framework of the world accounting concept of international accounting, Fantl theorizes that a worldwide set of generally accepted accounting principles (GAAP) would be established. Uniform practices and principles applicable to all countries would be the ultimate goals of international accounting. Fantl's descriptive approach, involving all the principles and practices of all countries and recognizing a set of GAAP for each country, visualizes the accountant to be multiple-principle conscious in his approach to international accounting. The international accounting system would be regarded as a collection of coexisting systems of accounting, and the accountant would have to be sufficiently aware of each system to be in a position to assess its effects on financial reporting. Under Fantl's parent-foreign subsidiary concept, the accountant is concerned with the translation and adjustment of a subsidiary's financial statements to those of the parent, whose country is used as the reference point for adjustment purposes. The main problem in this case is, of course, the

translation of financial information prepared in accordance with one set of principles to information that is consistent with a different set of principles.

B. WORLD ACCOUNTING APPROACH

1. Adolf Enthoven's Concept

Adolf Enthoven [13:115] prefers the term 'accountancy' to 'accounting' and describes 'international accountancy' as a reference to

> The applicability [of accounting] by, and for, all countries for internal and external purposes. It is to be applicable within the international arena and to serve the purposes of better international accountancy normalization, comparison, and appraisals for various socioeconomic functions.

Professor Enthoven's definition evidently matches closely with Fantl's concept of world accounting and may be categorized accordingly.

2. A. K. Jennings' Concept

Alvin K. Jennings [17:36-41] has described international accounting as "the crucial standards of quality of professional practice" of accounting which could be accepted internationally. Incidentally, Mr. Jennings considers that these standards "do in fact exist and are essentially uniform and any differences which exist are technical and, in many instances, superficial." While most authorities would probably hesitate to share Mr. Jennings' optimism, clearly his comments on the meaning of international accounting are consistent with Professor Fantl's concept of world accounting.

3. James Mahon's Concept

James Mahon [18:33-37] has pointed out that variations in accounting principles and practices between countries are to be expected but that "there is basically one common accounting language." By this he means that double-entry bookkeeping, the balance sheet, and the income statement are the common and basic tools of accounting throughout the world. Mr. Mahon has suggested that improved accounting principles and auditing standards are needed to narrow the variations in accounting principles and practices that exist between countries. Mr. Mahon has emphasized the importance of effecting these improvements because these variations lead to material differences in net income, working capital, and other pertinent information significant to investors and creditors. Thus this researcher's objective is the achievement of accounting uniformity among all nations. This uniformity, he contends, has hitherto been frustrated by national differences in economic, business, and governmental objectives--including differences among the highly developed nations. He believes that the solution to the whole problem lies in bringing about improvements in accounting principles and auditing standards. In essence, Mr. Mahon's views are in harmony with Professor Fantl's concept of world accounting.

4. The Journal of Accountancy Editorial

In an editorial, The Journal of Accountancy [19:32] has supported the establishment of a broad set of standards which would be acceptable to the accounting professions of

all countries. The editorial states that difficulty arises in interpreting financial statements of firms in foreign countries because of the variety of accounting and auditing principles and procedures that are now in existence. Since the main point of the article is the establishment of broad standards of accounting and auditing that would be acceptable to all countries, it would be appropriate to classify The Journal of Accountancy's viewpoint under Fantl's concept of world accounting.

5. Zimmerman's Concept

Professor Vernon K. Zimmerman has been quoted as saying that "international accounting could be considered as an abstraction of the highest order of accounting." [3:87]. By this statement Zimmerman presumably visualizes an accounting structure of universal theories which would transcend the limits of national boundaries. Although Zimmerman's concept recognizes a set of theories "that would be applicable to any phase of accounting in any country" [3:87] he has, however, pointed out that, at present, the term 'international accounting' has not been accorded a definition which has received international acceptance. Zimmerman's view of the matter is clearly the same as Fantl's first category, that is, world accounting.

C. DESCRIPTIVE APPROACH

1. Mueller's, Walker's and Berg's Concept

Professors Mueller, Walker and Berg [15:2] have offered this definition of international accounting:

> International accounting, as we use the phrase, (1) is concerned with international implications of the various national accounting thoughts and practices, and (2) measures and communicates, in financial and economic terms, international business events and transactions.

Since this definition embraces all the various accounting practices and concepts, it is essentially the same as the second of Fantl's three alternatives described above, namely, the descriptive approach.

2. Mueller's Concept

Gerhard Mueller, throughout his book, International Accounting [2], has emphasized that international accounting concerns the interrelationships of accounting among countries. He recognizes that there are differences in accounting procedures and practices among countries, and that international accounting is the study of these differences and their interrelationships. This concept of international accounting agrees with Fantl's descriptive approach.

3. Kollaritsch's Concept

Professor Felix P. Kollaritsch [20:382] considers international accounting to include all the various accounting principles and practices of all countries. His view of international accounting, like Mueller's, therefore also may be categorized with Fantl's descriptive approach.

D. PARENT-FOREIGN SUBSIDIARY APPROACH

1. C. C. Bowles' Concept

C. C. Bowles [16:85] regards international accounting as the accounting problems and practices of multinational operations. Bowles dwells at length on the interpretation

and translation problems of financial communication between parent and foreign subsidiaries. Some of the problems indicated were the vast variety of measuring units, both physical (e.g., gallons and litres) and monetary (e.g., dollars and francs), and the different tax structures and depreciation rates. Mr. Bowles' concepts coincide with Fantl's third category mentioned above.

E. NO INTERNATIONALLY ACCEPTED DEFINITION

From the research efforts to date, including those of the International Accounting Standards Committee, it is clear that the term 'international accounting' has not yet received a definition that is accepted by all nations or even within the same nation.

> If we as accountants are striving toward the goal of improving the development of accounting on an international basis, then it is only logical that we all start from the same point, the development of one internationally accepted definition of the term international accounting. . . .if accountants are going to use the term 'international accounting', then we should take upon ourselves the responsibility of arriving at a definition which has universal agreement and acceptability. [3:87].

The goal of improving the development of accounting on an international basis is increasingly being recognized as a tremendous challenge to the accounting professions of all countries. The activities of international congresses of accountants, and the committees which these congresses have created, are evidence of this fact. The activities of these bodies will be dealt with in a subsequent chapter. This challenge is one that many believe the accounting professions of the world must meet without having to seek the support or intervention of

governments, legislatures, or other agencies of the state.

As Stephen Zeff has written:

> I cling to the belief that accounting principles should be established by agencies in the private sector, preferably professional accounting societies, not by governmental fiat, whether through legislation, presidential or judicial decree, or administrative regulation. Surely, the result would be more responsible to societal needs and less fettered by bureaucratic intrigue, political pressure . . . [21: Preface, p. viii).

The derivation of a uniform definition of the term 'international accounting' is the first step which the accounting professions of the world must take to meet this challenge. Until they can succeed in doing so, perhaps the interim approach suggested at the beginning of this chapter, of working with Fantl's three concepts, would be more meaningful than the confusion of terminology that presently exists. It has been suggested in this chapter, by referring to the concepts of international accounting as viewed by various writers, that it should be possible to narrow the range of concepts to the three proposed by Fantl. But until a uniform definition acceptable to the accounting professions of all countries is available, its absence would remain one of the problems confronting research in the area and all that that implies.

III. THE EXISTING INTERNATIONAL NONUNIFORMITY--GENERAL EXTENT

International variations in accounting practices cover a rather wide spectrum. It should be a matter of no great surprise that the differing economic, social, political and cultural environments discussed in Chapter I have been sufficiently formidable to create these variations even among such countries as Canada, England, Scotland and the United States. In this context, Professor Gerhard Mueller has written:

> Despite an unquestioned international heritage, accounting has been singularly unconcerned with its international dimensions for the past hundred years. While other disciplines have established close international working relationships, accounting has tended to become nationalistic in its approach and outlook. [2:Preface]

The wide variation in accounting standards which at the present time exist in different countries is substantially evidenced in a booklet entitled Guide to the Reader of Foreign Financial Statements, which was published in June 1971 by Price Waterhouse and Company. [4:66]. It analyzes the differences in accounting principles and practices between the United States and 24 other countries and classifies these differences as major and minor items, both with regard to accounting measurement principles and also to matters of disclosure. The nature of the differences is described briefly in each case, and it is remarkable how much variation there is even when the allegedly "objective" historical cost basis is used. [4:64-67]. Even more descriptive is the AICPA's Professional Accounting

in 30 Countries, which also compares the accounting procedures and practices of the countries covered therein with those of the United States. [8].

Tradition wields a powerful influence in shaping not only the opinions of people but also the more tangible matters concerning business practices. Not only accounting procedures but, even more so, the attitudes of the public toward the accounting professions in various countries vary widely. For example, Swedish accountants seem confident that the economic stability of their country owes much to their practice of maintaining the uniformity of corporate profits through the manipulation of secret reserves, of which Professor Gerhard Mueller, in a letter to the author, has this to say:

> Key methods for building up secret reserves include (1) translating foreign exchange holdings at artificially low exchange rates, (2) overstating allowances for bad debts, (3) understating inventory amounts, (4) overstating depreciation, depletion or amortization allowances, (5) premature write-off of fixed asset amounts, (6) non-recognition of various intangible assets, (7) overestimation of actual liabilities, and (8) overstatement of contingent liabilities. Respective dissolutions of such secret reserves simply reverse the original bookkeeping mechanics, i.e., stating foreign exchange balances at their realistic exchange value--and thereby either showing a foreign exchange gain or a lesser foreign exchange loss in the income statement or stating doubtful accounts at an economically realistic valuation--and thereby avoiding current bad debt expenses and thus increasing current income, etc., etc. Companies utilizing secret reserves often have as many as two or three dozen items to which such reserves apply. They then manipulate different items of this type in different periods so as to achieve the profit and loss targets they establish for themselves. This, I am sure you agree, has some fairly significant financial information consequences. [22].

In commenting on the Swedish practice, Irving L. Fantl has written: "Like Joseph in the Bible, they borrow from the fat

years to fill the needs of the lean years, instilling confidence in the populace." [5:15]. Fantl goes on to suggest that this system has proved to be both practical and successful in Sweden's socialized form of government control. On the other hand, many Latin American accountants seem to feel no social responsibility, their first concern being to comply with legal requirements for the satisfaction of auditors and to employ various techniques in the maintenance of the records with the sole purpose of avoiding tax liability. The accounting profession in these countries is understandably not held in high esteem.

The low status of the Latin American accountants is further evidenced by the fact that the educational requirements for entry into the profession are not very demanding. For example, the Tecnico em Contabilidade (bookkeeper) of Brazil is required to be a graduate of a recognized "escda tecnica de comercio," which is substantially the equivalent of the U.S. commercial high school. [8:79]. With this qualification, the tecnico is authorized under Brazilian law to sign the financial statements and other accounting documents of closed corporations, limited liability companies, and partnerships. The contador (accountant) must be a graduate of a recognized university offering an approved four-year curriculum which includes economics, business administration and accounting. The contador is, of course, authorized by law to sign the same types of financial statements as the tecnico. [8:80]. Incidentally, there is no regulation in Brazil which requires corporations in the private sector to

have their financial statements examined and reported on by an independent public accountant.

In marked contrast, membership of the Institute of Chartered Accountants of England and Wales requires the fulfilment of the following criteria: [8:603].

a. Membership in one of the chartered accountant student societies which arrange lectures on accounting subjects and classes for instruction.

b. A degree at a recognized university, or two passes at an advanced level of the General Certificate of Education plus an academic year at a recognized institute.

c. For graduates of U.K. universities, a period of three years, and for nongraduates, four years of practical training in the office of a chartered accountant in public practice plus an academic year at a recognized institute. This training period is governed by a training contract whose terms are approved and supervised by the institute.

d. For all student trainees, successful attempts in the Foundation, Examination, Professional Examination I, and Professional Examination II, which include bookkeeping, financial decisions, auditing, taxation, executorship and trusteeship, costing, law, economics, statistics, and general financial knowledge.

e. 22-26 Weeks' study leave during the training contract for correspondence course study, review, etc.

With such exacting requirements, it is hardly surprising that in the United Kingdom the prestige of the Institute is

very high, to the extent that the Department of Inland Revenues places immense confidence in a tax return filed by a chartered accountant and rarely questions it. Such confidence is a sure measure of the high repute of the British accounting profession. These differences are an interesting reflection on the temperamental and cultural variations between these peoples. [5:16].

The differences in disclosure practices, the absence of uniformity in the application of principles and the use of semantics, and the diversity of motivations behind the purposes of disclosure practices, all go to make the interpretation of financial reports of other countries extremely hazardous not only for the uninitiated but even for experts. For the foreign investor to determine the true financial position of some foreign concerns is further complicated by the loopholes for secretiveness offered by the different laws and accounting practices of some countries. While it is proposed to cite a few actual examples of disclosure distortions at a later stage, suffice it to say for the present that it has been asserted by some experts that financial disclosures which do not indulge in concealing asset and liability values, performance data, sales and operating expenses, investments and other relevant information, "are the exception rather than the rule." [7:67-70].

The basic explanations offered for these distortions is that managers in many countries prefer to operate in secrecy, and this is facilitated by the considerable latitude in preparing financial statements available to them in the laws and accounting practices of those countries. When a firm is in financial

trouble it has the option of resorting to a number of concealment techniques which are supported by different laws and a diversity of motives. In addition to the practice, indicated above, of presenting fictitious profits by drawing upon secret reserves, these techniques also include the following:

1. Placing high values on scrap and unsalable goods.
2. Covering operating losses by showing as ordinary income the non-operating income that comes from the sale of fixed assets.
3. Further distorting net income through accounting practices that have the effect of changing asset valuation and depreciation without notice.

A notable example of the latter practice is in the Soviet Union, where replacement costs rather than historical costs are carried in the books and depreciation rates are applied on a straight-line basis to an estimate of replacement value plus an estimate of 'intermittent major repairs' [10:50] over an estimate of the life of the asset. Each of these estimates is handed down to management from above by some department of government. The estimates of replacement value and of capital repair costs are, independently of each other, subjected to arbitrary revaluations. The expected life of assets are also revised on an arbitrary basis. [10:49-74]. While it is recognized that the life of a fixed asset is a matter of subjective judgment in any accounting system, as is also replacement valuation wherever it may be an accounting practice, the frequent or unpredictable revaluations in Soviet accounting must lead to many distortions in their accounts.

In the <u>Declining Art of Concealing Figures</u>, Robert Ball says: "The road to full and accurate disclosure is made particularly tortuous by the traditional bookkeeping habits that hang on abroad." [7:67-70].

In order to understand the problems of international accounting, it is necessary and desirable to bring into some sort of perspective the extent of the nonuniformity that prevails among the accounting principles and practices in the present-day world. While this is only an attempt to draw attention to the salient features of a highly complex panorama, the various details, shades and blendings that comprise it may be found in the AICPA's monumental presentation of the accounting systems of 30 countries [8] and in similar works produced by international accounting firms, the International Finance Corporation (IFC), and others. In the paragraphs to follow, a few of the most significant diversities are presented.

A. DIVERSITY OF VIEWS ON THE PURPOSE OF FINANCIAL STATEMENTS

Accountants, businessmen and others throughout the world have different concepts regarding the objectives of financial statements. These concepts vary widely from country to country. Unless some broad consensus on this fundamental issue can be achieved, it would surely be an exercise in futility to proceed further on the road to international uniformity.

An interesting distinction between the purpose of financial statements in Australia and those in the United States has been drawn by William P. Hauworth II, a partner of Arthur Andersen & Co., Chicago. [9:24-25]. He cites the overriding

requirement of Australian financial statements, as expressed in Accounting Research Study Number 3, published in 1972 by the Accountancy Research Foundation in Australia. It states:

> The overriding objective of financial reporting as now interpreted is to disclose all information necessary to provide a true and fair view of the state of affairs of a particular entity as at the end of the period of accounting and of the profit or loss it earned during the period of accounting. [32]

Mr. Hauworth contends that the objectives of financial statements in the United States, as expressed in Accounting Principles Board Statement Number 4, differ from those of Australia. This statement says:

> The objectives of particular financial statements are to present fairly in conformity with generally accepted accounting principles (1) financial position, (2) results of operations, and (3) other changes in financial position.

Mr. Hauworth considers the following point of difference to exist in the interpretation of the two pronouncements indicated above.

> At first glance this view of the objective of financial statements appears similar to the one held in the United Kingdom and Australia. The idea of presenting fairly is fundamentally the same as the idea of providing a true and fair view. However, APB Statement Number 4 goes on to specify four conditions that must be met in order to present fairly, in conformity with generally accepted accounting principles. These conditions, in effect, only require conformity with generally accepted accounting principles, and make no reference to a fair presentation or a true and fair view. Thus, while in the United Kingdom and Australia the overriding objective of financial statements is considered to be providing a true and fair view, in the United States the APB apparently considers it to be to conform with a set of rules. [9:25].

Since Mr. Hauworth wrote these lines in The International Journal of Accounting in 1973, the Auditing Standards Executive Committee has issued a Statement on Auditing Standards

elaborating on the meaning of "present fairly in conformity with generally accepted accounting principles." This elaboration does not alter the thrust of Mr. Hauworth's argument, which appears to be valid as long as Australians do not define 'true and fair' to mean simply conformity with generally accepted Australian accounting principles. Mr. Hauworth has ascertained or assumed that no such restrictive definition exists in any of the professional pronouncements of Australia's accounting profession, and none of the available literature examined in the course of the present enquiry has revealed anything contrary to Mr. Hauworth's findings.

There are also countries where little thought has been given to the purpose of financial statements. In some such cases, the practice seems to be confined to compliance with government laws regulating companies (commonly referred to as Companies Acts) as to format and information required. In other cases, tax avoidance or other results considered by management to be in a company's best interests is deemed to be the purpose of financial statements.

In accounting literature the opinion has been expressed that financial statements prepared with the sole purpose of complying with company legislation or in order to achieve management's aims usually fall far short of providing a true and fair view or of conforming with generally accepted principles as developed by most accounting professions [9:25]. The opinion has also been expressed that accounting professions alone, rather than legislation, should establish accounting concepts. [21:Preface].

Only, therefore, if a set of commonly agreed objectives of financial statements are internationally defined and criteria are set up against which they can be evaluated can a theoretical framework of common principles be developed. [9:26].

B. VARIATIONS IN INVENTORY ACCOUNTING

Of the specific variations that flow from the wide spectrum of accounting concepts, perhaps that which has the most significant single effect on the results of operations and financial position of an entity is the method of inventory pricing. In the first place, there is a wide range of interpretations as to the constituents of cost. While in the United States and the United Kingdom full absorption costing is the general practice for financial statement purposes, in continental Europe, and especially in Italy, some or all elements of indirect cost are excluded. In France, according to Mueller [2:227], the 'Plan Comptable General' includes or excludes certain cost elements by definition. Mueller has not identified these elements, and the AICPA's description of the plan does not indicate these cost accounting details. [8:209].

Furthermore, cost flow assumptions differ widely. Although first-in, first-out (FIFO) is probably in greatest vogue, many others have also found frequent acceptance. Although last-in, first-out (LIFO) is found in a number of countries, it is not in frequent use anywhere but in the United States. The French Plan [8:211] uses the average cost method most frequently, although FIFO and specific identification are also sometimes used there. The Netherlands [8:406] permits any systematic method.

Table I contains a presentation of the inventory cost flow methods employed in a sampling of eighteen different countries.

TABLE I

Cost Flow Assumptions for Inventory Valuation

Country	METHOD			
	FIFO	LIFO	Average	Specific Identification
United States	X	X	X	X
Argentina	X	X	X	X
Belguim	X			
Brazil	X		X	
Canada	X		X	
Chile			X	
Columbia	X		X	X
France	X		X	X
Israel	X		X	X
Italy	X	X	X	X
Mexico	X	X	X	X
The Netherlands	X	X	X	X
Nationalist China [26:86]	X	X	X	
Peru	X	X	X	X
The Philippines	X	X	X	X
Sweden	X			
West Germany	X	X	X	X

Note: All data obtained from AICPA's Professional Accounting in 30 Countries [8] except where otherwise indicated.

The variations in accounting practices that depart from cost are also numerous. The lower-of-cost-or-market rule is a universally employed practice. The difference lies in whether it appears in conjunction with other inventory measures,

as an alternative to other inventory values, or as a valuation principle for all assets. The key to this rule lies in the definition of the term "market". In the United States the replacement or reproduction cost definition prevails [8:666], in contrast to the net realizable value interpretation in the United Kingdom [8:616] and Australia [2:228]. A combination of both is used in Canada, where the net realizable value concept is applied to finished goods and the replacement or reproduction cost concept to work in process and supplies. [8:211].

In the Netherlands replacement cost is used with such regularity as the primary basis of inventory valuation that it may be regarded as a generally accepted Dutch accounting principle. [2:229]. In Austria [2:229], Italy [8:309], and Japan [8:334] inventories at historical cost are adjusted for price-level change by means of price indices promulgated by the government, while in Sweden [8:560] this is done only for certain raw materials and staple commodities. In some countries, such as Japan, the government promulgates different price indices for application to different types of inventories. The price-level adjustment methods vary from complete inclusion in the cost of goods sold figure to complete separation and reflection in the owner's equity section of the balance sheet.

Some countries, including Denmark and Switzerland, permit arbitrary percentage reductions of inventories, the amounts of which reductions may be changed from year to year. This practice opens a Pandora's box of manipulations which facilitate sweeping portions of profits under the rug in certain periods

for retrieval later in unprofitable periods. This is achieved in Switzerland, for example, through the mechanism of secret reserves, referred to earlier. In Switzerland the law does not require disclosure in the annual accounts on the basis of which assets are valued. Company law specifically permits management, at its discretion, to undervalue assets in the balance sheet and to carry the understated amount in a secret (also called undisclosed) reserve. The law permits the release of amounts from the reserve for the purpose of enhancing reported net income. The existence and the amount of an undisclosed reserve, and the amount set aside or released in the year, need not be reported. [8:590-591]. In discounting any justification for the creation of secret or hidden reserves, the first International Accounting Standard (IAS 1), issued by the International Accounting Standards Committee (IASC), has given recognition to the fact that, when secret reserves are permitted, one can never be sure of the accuracy of reported profits. [11:para 9a].

The overall impact on financial statements of this maze of inventory pricing practices does not appear to have been subjected to any systematic research, but it may be reasonable to assume that the impact could be significant.

C. TREATMENT OF FIXED ASSETS

In the United States, the United Kingdom, Canada and Australia the accepted basis of carrying plant property on the balance sheet is historical cost, with depreciation charged as an expense on a periodic basis according to some recognized method.

However, it appears that the United States is the only country which does not allow variations to this practice. Australia [8:44] allows upward revaluation and recording of the resulting credit as a "capital revaluation reserve" and the United Kingdom [8:616] follows a similar practice.

The accounting treatment of fixed assets in the Soviet Union has been outlined earlier in this chapter. It contrasts with those of the above three countries mainly by virtue of the inclusion of estimated repair costs in fixed asset valuations, the arbitrary revaluations of these estimated repair costs and of replacement costs, the arbitrary revision of the expected life of fixed assets, and the consequent fluctuations in the amount of straight-line depreciation charged from period to period as a result of these revaluations and revisions.

In Brazil, as stated earlier, fixed assets are revalued because of Brazil's inflation problems. In that country, and also in Argentina [8:29], all large business entities registered under law are required under the relevant statutes to revalue their fixed assets annually according to coefficients fixed by government. [8:88].

In Switzerland, assets may be revalued but at not more than their value to the business [8:588]; this subjective criterion leaves a wide range for manipulation. Other countries whose laws permit the adjustment of historical costs in asset revaluation include Japan, Italy, Argentina, Belguim, France, West Germany and Peru. Thus, in various countries property is carried in the accounts at current replacement cost, at

appraised value, at historical cost, and at at historical cost adjusted to reflect currency devaluation. Also, depreciation methods vary widely and often include methods not followed in other countries. Table II illustrates some of these variations in depreciation practices.

TABLE II

Depreciation Methods in Practice in Some Countries

Country	Method of Depreciation			
	Straight Line	Declining Balance	Sum-of-the-Years Digits	Productive Output
United States	X	X	X	X
United Kingdom	X	X		
Soviet Union [25:144]	X			
Israel	X			
Japan	X	X	X	
Spain	X			
Norway	X	X	X	X
Argentina	X	X	X	X
Greece	X			
Chile	X			
Italy	X	X		
The Netherlands	X	X		
Lebanon	X			
France	X	X		
Columbia	X	X		
India [24:42]	X	X		

Note: All data obtained from AICPA's Professional Accounting in 30 Countries [8] except where otherwise indicated.

D. UNDERSTATEMENT OF ASSETS AND OVERSTATEMENT OF LIABILITIES

In some countries it is permitted by law for assets to be systematically understated and liabilities systematically overstated. For example, some countries allow the creation of inventory reserves which are arbitrarily determined by managements or by provisions of income tax laws. As noted earlier, Switzerland is an outstanding example of this practice [8:590], and Sweden also permits it [8:560]. In both countries, in addition to legal reserves, the maintenance of secret reserves, derived from the understatement of assets is lawful. But these are not the only countries. Other countries permit arbitrarily high allowances for bad debts on receivables. Still others regard as acceptable unusually high provisions for future liabilities. In this context, the laws of Italy and India seem to provide much latitude for overstating liabilities. The Companies Act of India makes special provision for management's discretion in deciding the amount of a liability when in their opinion "the amount cannot be determined with substantial accuracy" [8:272]. Italy's Civil Code, which prescribes the contents of the balance sheet and the principles of valuation of assets and liabilities, provides a long list of liability accounts, including such nebulous titles as "other reserves" and "other liabilities" [8:308].

The problem for the foreign investor arises not merely from these varied locally accepted practices but also from the fact that they are not disclosed at all, or not in a manner that would facilitate an assessment of their effects on financial position and operating results [2:220].

E. VARIATIONS IN INCOME TAX RECOGNITION IN ACCOUNTS

Income tax payments required by law are significant in nearly all countries and affect small as well as large business firms. Even the state of economic development of a country does not seem to have much to do with this fact. For example, corporate income tax rates are higher in India than in the United States, whose corporate income tax is rated high by international standards. The impact of corporate income tax requirements is substantial, and there are international variations in recognizing tax effects in accounts.

The following bases for recognizing income tax effects are to be found in various parts of the world:

1. The cash basis of recognition.
2. The accrual basis of recognition.
3. Tax allocation procedures.

1. Cash Basis

Argentina [8:17, 2:230] is an example of cash basis accounting for income taxes. The companies laws of that country provide for accounting recognition of income tax only after it has actually been paid. Only the taxes actually paid are reported in the income statement. Cash-basis accounting is also extensively in use in developing countries where industrialization, and therefore accounting, are still in a formative stage and where, due to uncertain tax collection enforcement, the process of estimating tax liabilities is almost impossible. Also, in these countries companies often do not publish financial statements for general third-party use. Management, creditors

and a close group of stockholders, already have all the financial information they need, including the tax status of the enterprise because they work with internal reports. Under these circumstances, internal oriented cash-based income tax reports are sufficient and reasonable [2:231].

2. Accrual Basis

The accrual basis of income tax recognition wherein, irrespective of due or actual dates of payment, taxes payable currently are estimated and accrued in the financial statements of the period to which they are attributable, is prevalent in Germany, Sweden and most other European countries and also generally in the Far East, including Japan, the Philippines, and South Korea [2:231]. Full accrual recognition in the financial statements of these countries is achieved by expensing the estimated income tax in the income statement of the period of incurrence and by showing it as a current liability in the corresponding balance sheet.

3. Tax Allocation

Lastly, there are the tax allocation procedures of the United States. These procedures are also practiced in the Netherlands and, to some extent, in Canada and the United Kingdom; and they have made an appearance in several other countries, including Australia [8:44-45], Israel [8:292], Japan [8:338] and Sweden [8:564]. The Dutch practice originated with the large number of corporations from that country selling shares of stock in the United States capital market and, therefore, coming under the regulations of the U.S. Securities and

Exchange Commission. Of course, these Dutch corporations had to issue financial statements for the benefit of their United States stockholders. Thus, they were drawn into use of the generally accepted accounting principles of the United States. The income tax allocation procedure of the United States arises from a difference in the timing of recognition of certain expense and revenue items on the income statement as opposed to the income tax return. This constitutes a significant international accounting variation regarding the recognition of income taxes in accounts.

These varying income tax recognition bases, as may be expected, are bound to make a material difference in reported financial results.

F. EQUALIZATION OF REPORTED INCOME OVER SEVERAL ACCOUNTING PERIODS

The generally accepted accounting principles of the United States and many other countries require that the costs of generating particular revenues be matched with those revenues in the period in which they are earned. That is to say, that periodic profits or losses should be a clear reflection of revenues and their matching expenses of a period. There are, however, countries which permit practices designed solely for the purpose of equalizing reported profits over more than one accounting period. Sweden's practice [8:561] of utilizing reserves for this equalizing process has already been cited. Other European accounting systems, including France's 'Plan Comptable General' [8:213] and West Germany's Companies Act,

which regulates that country's accounting practices in considerable detail [8:722, 739], also allow reserve accounts. Belguim's [8:66] and Switzerland's [8:590] laws allow secret reserve accounts. The reserve accounts of all these countries are permitted to be used for the purpose of reporting uniform profits.

G. GAINS AND LOSSES EXCLUDED FROM STATEMENT OF INCOME

In some countries it is generally accepted or is even legally required to exclude from the determination of net income items such as profits on sale of properties or investments, bonuses paid to management personnel and directors, and taxes on income. In those countries, such items are not shown on the income statement [2:220], and the disclosure practices of such transactions vary widely. In Italy, for example, the payment of bonuses to directors is generally charged to a "surplus account" which is seldom presented [8:311]. In Venezuela, a separate "statement of distribution of profits" is frequently prepared and in this statement the payments of bonuses to management and directors, income taxes, etc. are shown, instead of in the "Statement of Income" [8:708]. In other words, in Venezuela, while these payments do not determine net income, they are distributed from net income. An approximately similar practice is also followed in Belgium.[8:67].

H. OTHER VARIATIONS

Considerable variations in underlying theories and semantic differences remain. In an article appearing in <u>Business Horizons</u> under the caption 'International Differences in Disclosure Practices,' Jeffrey S. Arpan [7:67-70] states that a 'current liability' in some countries has different meanings. In the same context he refers to the Dutch 'latent liability' without defining it. Since Dutch accounting principles and practices [8:401-412] do not appear to recognize the term 'contingent liability' which immediately suggests itself, 'latent liability' is evidently not the Dutch synonym for 'contingent liability.' Perhaps 'latent liability' refers to the Dutch:

> Voorzieningen, or provisions relating to specific assets if not otherwise deducted from those assets, provision for deferred or contingent tax liabilities and provision for pension obligations. [8:404].

The very fact that a conjecture has to be made as to the significance of this term, because verification from all reasonably accessible sources has failed to clarify its meaning, is an illustration of the fact that differences in accounting semantics lead to areas of uncertainty for the users of foreign financial statements.

Even if the disclosure is forthright, an anlyst has to beware of more subtle differences which often cumulate into substantial amounts in monetary terms [7:67-70].

To present a few notable variations in perspective, the following generally accepted accounting principles relied upon in the United States are not usually followed elsewhere.

1. In the preparation of consolidated financial statements the parent company is subordinated to the entity taken as a whole. In the United Kingdom the Companies Act permits the directors of a company to authorize variations from the presentation of consolidated financial statements, which variations have the effect of presenting the parent as the entity and the subsidiaries as appendages or branches of the entity. For example, the parent's financial statements may be accompanied by those of the subsidiaries referred to as "group" accounts. In West Germany, the Companies Act permits the omission of a subsidiary from consolidation when management considers that the subsidiary is insignificant [8:736]. In India, where consolidation is optional under the Companies Act, the parent or 'holding' company's report may, as an alternative to consolidation, be 'accompanied' by those of the subsidiaries [8:269]. In New Zealand, with the consent of the Governor-General by Order in Council, or in certain prescribed cases under the provisions of the Companies Act, a subsidiary may be excluded from the consolidated accounts and the holding company's investment in the subsidiary must be reflected separately in the consolidated statements [8:429]. Each of these variations emphasizes the parent rather than the entity as a whole. In France, evidently the law permits the submerging of the results of operations of subsidiaries altogether. An example of this nature is Michelin, the French tire and rubber giant, which omits the results of operations of its many subsidiaries by not publishing any consolidated financial figures [7:68].

Jeffrey S. Arpan [7:70] has emphasized that the most significant procedure practiced outside the United States, but not in the United States, concerns consolidation policies. He states:

> But if there is one single procedure that renders most non-American corporate reports meaningless, it is the failure to consolidate the operations and financial positions of subsidiaries with those of the parents. This omission can conceal profit-and-loss developments of substantial size, in addition to significant changes in claims and liabilities between members of the corporate family. It is particularly critical when the parent companies are holding companies as well as operating companies, which is the case for most non-American multinational firms. The alteration of no other single procedure would improve the reliability of their financial reports as much as this one. [7:70].

However, as illustrated earlier in this chapter, a number of countries do require parent-subsidiary consolidation, although there is some variation in the procedures involved. Arpan's statement that most non-American corporations fail to consolidate financial statements with those of their subsidiaries is perhaps an overstatement.

2. In the United States, stock dividends are accounted for at fair market value of additional shares distributed. In the United Kingdom [8:620], West Germany [8:739], and France [8:214] stock dividends are accounted for at par by the issuer [8:620]. In New Zealand stock dividends are accounted for by the issuing company 'on the basis of the paid-up value of the shares, without consideration being given to market or fair value thereof' [8:434].

3. In the U.S. there are precise conditions under which a business combination <u>must</u> be measured and reported as a

pooling of interests, and all combinations not meeting the specified conditions must be accounted for by the purchase method. These conditions are stated in APB Opinion No. 16 [50]. The absence of any formal distinctions between purchases and poolings and the absence of recognition of poolings in many countries are significant departures from the practice in the United States. In Canada no pronouncement on the treatment of "pooling of interests" has been made, and financial statements presented in this manner have not been governed by any criteria. [8:117]. "Poolings" are not recognized in the accounting systems of Australia [8:45], Belgium [8:66], Italy [8:309], South Africa [8:526], Mexico [8:377], and a number of other countries.

On the other hand, the following procedure is permissible in other countries but not in the United States.

Legal reserves to prevent dividend payouts on the basis of reported net income from operations or on the basis of debt-equity ratio as stipulated. This means that the amount of the dividend to be paid in a given year may be limited to the amount of net income or to a proportion thereof, or to an amount such that the debt-equity ratio does not exceed a certain proportion. For example, it may be decided that the debt-equity ratio, the proportion of creditors' equity to owners' equity (contributed capital plus retained earnings), shall not exceed 0.50. Given the following figures:

Total Liabilities (creditors' equity) . . . $ 100,000
Contributed Capital 175,000
Retained Earnings 75,000
The debt-equity ratio at present is $\frac{\$\ 100,000}{\$\ 250,000} = 0.40.$

The limitation therefore restricts the dividend payout to $50,000. If the maximum limit of $50,000 is availed of, the position would be:

$$\text{Debt-equity ratio} = \frac{\$\ 100,000}{\$\ 175,000 + \$\ 25,000} = \frac{\$\ 100,000}{\$\ 200,000} = 0.50.$$

This procedure does not stipulate that the dividend payout shall not exceed the retained earnings. In the above example, if the contributed capital were $210,000 and the retained earnings $40,000, it would be in order to use up all of the retained earnings as well as $10,000 from the contributed capital without violating the rule of maintaining the debt-equity ratio at a level not in excess of 0.50. In the United States, the state laws place a restriction on such dividends, and corporations seldom disburse more than 50-70% of retained earnings as dividends [28:426].

IV. DISCLOSURE PRACTICES--A FEW ILLUSTRATIONS

A. THE IASC's FIRST CONCERN

In briefly recounting the complete absence of uniformity in accounting practices across international borders, reference was made to a few areas of accounting in which differing accounting policies exist and the nature of those differences. In fact, there are many more. A comprehensive list of 25 of these areas is contained in the introduction to International Accounting Standard I issued by the International Accounting Standards Committee (IASC) [11: para 13]. This list is reproduced as Table III. Of the activities of this Committee and its parent organization, the International Coordination Committee for the Accounting Profession (ICCAP), more will be said in a later chapter.

It is significant and not at all surprising that the IASC's first standard deals with the subject of disclosure, for it is in matters of disclosure that most of the trouble seems to lie. The incorrectness or inappropriateness of various disclosure practices, their variety, and the credibility gap which they may create are subjects worthy of extensive research. The illustrations of disclosure practices that follow are examples of the variety of those practices among nations. These illustrations also point to the sense of uncertainty and skepticism as to their reliability that can arise as a result of this lack of uniformity and also lack of forthrightness in many cases. These are only examples and are by no means exhaustive.

1. F. Hoffman-La-Roche

This Swiss company is one of the world's largest manufacturers of drugs. Most experts, including European, estimate that the reported earnings of Hoffman-La-Roche represent only 15% of their true consolidated earnings. The company discloses no sales figures, no detailed investment figures nor any meaningful cost figures. About all it does report is contained in an incredibly vague and meaningless statement from the Board of Directors:

> The results again show improvement over the year before. Sales and earnings increased in approximately equal proportions. The global development . . . shows a somewhat slower rate of expansion than in previous years but remains at a high level. . . . The volume of investment was again large, and will hardly diminish in the foreseeable future. [7:67-70].

This is not merely a case of insufficient details, which renders any kind of financial analysis and evaluation impossible; but it conveys a strong impression of an attempt to conceal and mislead the users. Evidently the Swiss law and the Swiss accounting profession are indulgent toward such minimal disclosure.

2. Rhone-Poulence

According to one estimate [7:68], Rhone-Poulence, the large French chemical manufacturer, shows earnings one-fourth of its true earnings.

3. Others

Other famous firms which are shy of disclosing their true financial positions include Nestles, Compaignic de Saint Gobian, Pechiney, Schnedler, Pont-a-Moussoon and Cie, and General d'Electricite. [7:70]. Of Sanyo Special Steel Company

of Japan it was alleged that, by understating or not disclosing the full extent of its liabilities it was able to escalate those liabilities to ten times the book value of its capitalized assets of $22 million before going bankrupt. [7:70].

4. <u>"More Honest Than They Need Be"</u>

Jeffrey S. Arpan has said that some firms are "more honest than they need be." [7:70]. Although Arpan has not elaborated upon the criterion for needed disclosure, beyond which disclosures become "more honest than they need be," the accounting profession in the United States has amply expanded on this subject through the literature. Basically, two points are emphasized.

a. Generally, immaterial information should not be disclosed:

> Disclosure is needed only for material facts. The concept of materiality as used in accounting has been defined as a state of relative importance. Unfortunately, there is no handy rule of thumb to tell us whether a given item is material. . . Both quantitative and qualitative elements warrant consideration in the determination of materiality. . . In achieving adequate disclosure it is important not to clutter up the statements with unimportant details. [30:24].

b. Together with excessive detail is the question of disclosures that may harm the interests of a business. "Disclosure should not be considered to require publicizing certain kinds of information that would be detrimental to the company or its shareholders." [29:430.05]. For example, premature disclosure of a prospective merger might injure a company's position, or the disclosure of an out-of-court settlement of a single pending lawsuit among a number of interrelated suits might also prove injurious to the company.

All this leads to the conclusion that the extent of disclosure is a matter for subjective judgment, and the accounting profession in the United States has recognized this fact:

> What constitutes a matter requiring disclosure is for the independent auditor to decide in the exercise of his judgment in the light of the circumstances and facts of which he is aware at that time. [29:430.03].

Perhaps the management of the firms Arpan had in mind and their auditors did not in their judgments consider that they were divulging more than was necessary, in the light of the information known to them and the disclosure practices of their countries' accounting professions. However, none of this alters the fact that extremes in disclosure practices do exist. At one end of the scale are those firms that disclose too little. At the other end of the scale are those that may disclose too much.

The firms that Arpan considers to be "more honest than they need be" include Britain's Imperial Chemical, British Petroleum and Beecham Group; Holland's Philips and Royal Dutch Shell Group; Germany's Bayer, Hoogenuens and Hoeganaes; Sweden's L. M. Ericson; Switzerland's Lanes and Gyr. [7:68]. On the other hand, V.A.W., one of Germany's largest international aluminum companies, is said to publish an annual report of 50 pages containing colorful photographs, glib phraseology, and only one page of financial data.

The consensus of experts is that, if companies were to be ranked in order of authenticity and candidness of their reporting, the American, British, and German firms and the large Dutch and Swedish international firms would rank first.

A distant second group would include French, Swiss, Italian, Spanish, Belgian, and Japanese firms [7:68].

These cases, which are merely a sampling of worldwide practices, exemplify the variations of accounting disclosure practices among nations. They vary from the one extreme of being reluctant to disclose any meaningful data at all to the other extreme of probably revealing more detail than most users of financial statements require for the purpose of making financial evaluations. In the majority of cases, the basic explanations seem to lie in a preference of managements to operate in greater rather than less secrecy and in the variety of laws and accounting practices of different countries that give greater or less latitude in the preparation of financial statements. Naturally, the users of financial statements are very likely to attribute questionable motives to those managements whose financial disclosures betray a preference for secrecy through the use of various concealment techniques.

TABLE III

Paragraph 13 of International Accounting Standard 1: "Disclosure of Accounting Policies" -- [11:Para 13]

VARIATIONS IN ACCOUNTING POLICIES AND IN THEIR DISCLOSURE.

13. The task of interpreting financial statements is complicated by the adoption of diverse policies in many areas of accounting. There is no single list of accepted policies to which users may refer and the diverse accounting policies that are presently available for adoption can produce significantly different sets of financial statements based on the same events and conditions. The following are examples of areas in which differing accounting policies exist and which therefore require disclosure of the treatment selected:

General.

Consolidation policy.

Conversion or translation of foreign currencies including the disposition of exchange gains and losses.

Overall valuation policy (e.g., historical cost, general purchasing power, replacement value).

Events subsequent to the balance sheet date.

Leases, hire purchase, or installment transactions and related interest.

Taxes.

Long term contracts.

Franchises.

Assets.

Receivables.

Inventories (stock and work in progress) and related cost of goods sold.

Depreciables assets and depreciation.

Growing crops.

Land held for development and related development costs.

Investments: subsidiary companies, associated companies, and other investments.

Research and development.

Patents and trademarks.

Goodwill.

TABLE III (continued)

<u>Liabilities and provisions.</u>

Warranties.

Commitments and contingencies.

Pension costs and retirement plans.

Severance and redundancy payments.

<u>Profits and losses.</u>

Methods of revenue recognition.

Maintenance, repairs, and improvements.

Gains and losses on disposals of property.

Reserve accounting, statutory or otherwise, including direct charges and credits to surplus accounts.

V. INTERNATIONAL COOPERATION TOWARD A UNIFORM SYSTEM

A. THE EUROPEAN COMMON MARKET

The most purposeful effort which is at present being undertaken to narrow accounting differences among a group of nations is by the member states of the European Community to further the functioning of the Common Market. Harmonization of annual accounts within the EEC is considered essential by its members to facilitate the availability of comparable information on the capital, financial position, and results of operations of companies (1) for the benefit of prospective and established customers and suppliers undertaking the risk of commercial dealings among members, and (2) to encourage employment of capital within the community by an investor in a member state trading in the shares of companies of other member states. One would expect this project to take several years of difficult negotiation. [35:652]. In an article published in The International Journal of Accounting, Leonard M. Savoie, Vice President and Controller of Clark Equipment Company, has written:

> The European Common Market has the structure and the legal basis for establishing uniform accounts and they are making good progress in this direction. Their effort may well succeed in the Common Market and result in other countries adopting the same standards. Conceivably these standards could become the standards of the world. Should that happen, we may have to change U.S. principles, customs, and perhaps laws to comply with standards we had no part in shaping. If we took the leadership in working toward international standards, we would still have to make some changes but we could also play a major role in attaining the most appropriate standards. [36:21].

B. COOPERATION AMONG INDIVIDUAL ACCOUNTING ORGANIZATIONS--REGIONAL BODIES

The organization of professional accounting bodies in individual countries started over a century ago. It has progressed steadily in the interval, and today many countries in the world have well developed accounting professions responsible for standards, ethics and the education and training of members. This phenomenon set the stage not only for cooperation between accounting bodies developing at a comparable rate but also for assisting countries developing at a slower pace. Initially, regional conferences were held periodically for the exchange of information in the hope of finding solutions to mutual problems. These conferences resulted in the accounting bodies in Europe becoming linked through the medium of the Union d' Experts Comptables (UEC), those of North and South America through the Inter-American Accounting Conference (IAAC), and those of Asia and the Pacific through the Confederation of Asian and Pacific Accountants (CAPA). [37:37, 39:145]. While the objectives and methods of organization of all the above regional and inter-country activities vary, they all have the same common objective of furthering the understanding among professionals in different countries.

Substantial technical aid has been extended by many countries directly to other countries. Such aid has included the promotion of existing accountancy bodies and the formation of new ones, advice and assistance in the conduct of professional examinations, and the development of educational services. Technical information in the form of numerous professional

journals, research bulletins and other material is published by various accounting bodies; and the exchange of complimentary copies, as well as information regarding an organization, its policies and practices, has become customary [37:38].

C. ACCOUNTANTS INTERNATIONAL STUDY GROUP

An important step in the development of international accounting standards took place in 1966 when the President of the Institute of Chartered Accountants in England and Wales visited the United States and Canada. In consultation with the Presidents of AICPA and the Canadian Institute of Chartered Accountants, he established a three-nation study group called the Accountant's International Study Group (AISG). In the ensuing six years the AISG studied several important accounting issues affecting the three member countries and published studies on a variety of subjects [37:38]. It has been claimed that the work of the AISG contributed substantially to greater harmonization among the three countries [41:24]. It was, however, recognized at the time the AISG was set up that this was only a first step in a much longer concept. At the International Accountants Congress held in Sydney in 1972 the proposal to form the International Accounting Standards Committee came primarily from the AISG member countries. Of the latter Committee and the Congress which brought it into existence, more will follow later in this chapter.

D. INTERNATIONAL CONGRESSES OF ACCOUNTANTS

Out of the need for closer ties among the professional accounting bodies of the free world, several organizations have been formed to bridge the gaps among the different sets of accounting principles, auditing standards, and financial reporting practices in order to make accounting truly the international language of business. At each congress, conference or meeting, the call for more uniformity and greater harmonization is heard; and certain measures are adopted to achieve and maintain such a goal.

The International Congresses of Accountants are a significant and tangible effort in the direction of solving the persistent international accounting problems. [38:7]. The first International Congress of Accountants was held over 70 years ago. Since 1926, with a gap during World War II, Congresses have been held at about five-year intervals. The Tenth, held in Sydney, Australia, in October 1972, was attended by over 3500 participants from 60 countries. [38:38].

Frequently, and particularly in the past fifteen years, the theme of conferences has centered on harmonization of accounting standards, international standards of accounting, and other topics which go beyond the boundaries of any one country. The subjects tend to reflect the development of multinational corporations, the complexity of our society today, and the concern of the professional accountant with such topics as inflation accounting, financial statement preparation, and comparable matters.[38:38].

Table IV summarizes the salient facts concerning each of the International Congresses. Table V shows the attendance of individual countries at these Congresses.

TABLE IV

International Congresses of Accountants: 1904-1972

			Number of:		
No.	Year	Place	Participating Countries	Participants	Papers Delivered
1	1904	St. Louis, US	4	211	10
2	1926		15	370	25
3	1929	New York, US	23	1600	65
4	1933	London, England	20	160[b]	12
5	1938	Berlin, Germany	a.	a.	a.
6	1952	London, England	35	3519	35
7	1957		37	3000	29
8	1962	New York, US	51	3728	45
9	1967	Paris, France	59	4000	14
10	1972	Sydney, Aust.	60	3500	39

a. Proceedings not available due to the fact that it was held on the eve of World War II. Proceedings were probably destroyed.

b. Does not include participants from the host country.

Sources: Refs. 38:13 and 40:82.

TABLE V

Attendance at the International Congresses of Accountants: 1904-1967

Congress Country	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th
Argentina......						X		X	X	X
Australia......			X	X		X	X	X	X	X
Austria........		X	X	X		X	X	X	X	X
Belguim........						X	X	X	X	X
Bolivia........						X			X	X
Brazil.........						X	X	X	X	X
Burma..........						X	X	X	X	X
Canada.........	X		X	X		X	X	X	X	X
Ceylon.........							X		X	X
Chile..........								X	X	X
Nationalist China..........								X	X	X
Columbia.......						X		X	X	X
Costa Rica.....								X	X	X
Cuba...........			X							X
Czechoslovakia.		X	X	X						
Denmark........				X		X	X	X	X	X
East Africa....				X		X	X	X	X	X
Ecuador........								X	X	X
Egypt..........								X	X	X
Finland........		X	X			X	X	X	X	X
France.........		X		X		X	X	X	X	X
Germany........		X	X	X		X	X	X	X	X
Ghana..........							X	X	X	X
Greece.........								X	X	X
Hawaii.........			X							
Honduras.......			X							
Hong Kong......								X	X	X
Hungary........			X							
Iceland........			X							
India..........						X	X	X	X	X

TABLE V (continued)

Congress Country	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th
Indonesia......								X	X	X
Iceland........								X	X	X
Israel.........						X	X	X	X	X
Italy..........		X	X	X		X	X	X	X	X
Jamaica........								X	X	X
Japan..........			X	X		X	X	X	X	X
Korea..........								X	X	X
Lebanon........									X	X
Luxemburg......							X		X	X
Malta..........						X	X		X	X
Mexico.........			X	X		X	X	X	X	X
Monaco.........							X		X	X
Netherlands....	X	X	X	X		X	X	X	X	X
New Zealand....				X		X	X	X	X	X
Norway.........		X	X	X		X	X	X	X	X
Pakistan.......						X	X	X	X	X
Panama.........								X	X	X
Peru...........						X		X	X	X
Philippines....			X	X		X	X	X	X	X
Poland.........				X						
Portugal.......						X			X	X
Puerto Rico....			X					X	X	X
Rhodesia.......						X	X	X	X	X
Rumania........		X	X	X						
Russia.........		X	X							
Senegal........								X	X	X
South Africa...						X	X	X	X	X
Southern Rhodesia								X	X	X
Spain..........		X					X	X	X	X
Sweden.........		X		X		X	X	X	X	X
Switzerland....		X	X			X	X	X	X	X
Thailand.......							X		X	X
Trinidad.......							X	X	X	X

TABLE V (continued)

Congress Country	1st	2nd	3rd	4th	5th	6th	7th	8th	9th	10th
Turkey.........							X	X	X	X
United Kingdom.	X	X	X	X		X	X	X	X	X
U.S.A..........	X	X	X	X		X	X	X	X	X
Uruguay........						X		X	X	X
Venezuela......						X	X	X	X	X
Totals:	4	15	23	20	n/a	35	37	51	59	60

Note: The Fifth Congress was held in Berlin on the eve of World War II. The proceedings of this Congress are not available (n/a).

Source: Ref. 38:14-15.

It is notable from the latter table that the Soviet Union and the countries of Eastern Europe are conspicuous by their absence from all but the earliest congresses. It is not clear whether this is because these countries were not invited to attend or because they declined invitations to attend. At a time when the United States and the Soviet Union are cooperating in the highest field of human endeavor,. the space program, and cultural, commercial, and political contacts between the countries of Eastern and Western blocs are steadily increasing, it is a matter of surprise that there seem to be difficulties in the way of the accountants of all these countries getting together. This circumstance is rendered even more strange by the fact that Cuba, for all its hostility toward the West, found it possible to attend the Tenth Congress. Since the Peoples' Republic of China has long had commercial relations with many participating nations, and has now established them with the United States, it seems appropriate that it be invited to attend future congresses. It is considered that the International congresses are missing something of value by the absence of so many technologically advanced nations.

The following discussion highlights some of the significant aspects of these congresses.

1. <u>The First Congress (1904)</u>

At this congress, speakers pointed to the fact that:

> . . . an imperative need existed for unity of purpose and effort among practitioners and for a uniform standard of professional qualification and practice in every section of the United States. [38:7].

These matters were emphasized in every paper delivered at the congress. Among the subjects discussed were municipal accounting, the CPA movement, the future of the public accounting profession in the USA, the duties of professional accountants in connection with invested capital, and the mode of conducting an audit [38:7]. Apart from the fact that the First International Congress was represented by only four countries (United States, United Kingdom, Netherlands, and Canada), it will be seen that there was nothing very "international" about its proceedings. Indeed, the discussions apparently focused almost entirely on the accounting profession in the United States. But a start had been made, albeit a very modest one.

2. The Second Congress (1926)

The objectives of this congress were specified as follows: (a) To extend the benefits of the knowledge and experience acquired by the accountants in attendance to as large a circle of enterprises as possible. (b) To further mutual acquaintance among accountants and the uniformity of methods of working of accountants among various countries. (c) To propagate views that can be adopted internationally regarding problems concerning the science of cost calculations.

At this congress papers were reported in three languages--English, French and German. At this congress an interesting proposal was made: the establishment of an international prize, similar to Nobel prize for literature, for works on accounting subjects. Apparently nothing came of it. [38:7].

3. The Third Congress (1929)

The papers delivered at this congress were translated so that each paper was available in English, German and French. At this congress, Sir William Plender argued for frequent interchanges "of views and personal contacts with our professional friends, from whatever country they may come . . ." Papers were delivered at this congress on "Legislation and Education for the Accounting Profession" covering the profession in Austria, Cuba, England, Germany, Holland, India, Italy, Japan, Rumania, Switzerland and the United States. Other papers dealt with the practical problems of depreciation, principles of valuation, form and contents of financial statements, external influences affecting accounting practice, cost accounting, and the accountant's responsibility for the inventory [38:8].

4. The Fourth Congress (1933)

At this congress all papers were printed in English, with French and German interpreters present at the sessions. Because of the apparent need for much to be done to achieve worldwide auditing standards, Lord Plender, president of the congress, stated:

> It may be said that subjects of international interest have already been dealt with very fully in addresses and books which are available to the diligent speaker. But they are widely scattered and are not accessible to accountants in all countries, and not too readily found in the country of their origin. What is wanted is to bring together in concise and clear form essential material information concerning the relevant law and accountancy practice in each country as affecting matters of common interest to the profession throughout the world and to keep such information reviewed to date so that it embodies new legislation, recent decisions of the courts and the latest experience. Volumes so compiled would form a compendium of universal interest and be of great value to practitioners in each country. [38:8].

This suggestion had to wait 31 years before it was finally implemented by the AICPA Committee on International Relations in 1964, when a partial international survey of accounting and auditing theory and practice was presented in a book entitled Professional Accounting in 25 Countries.

This congress attended to problems relating mainly to international dimensions--international finance, exchange fluctuations, and holding and subsidiary companies.

5. The Fifth Congress (1938)

As this congress was held in Berlin on the eve of World War II and at the time of the Munich crisis, apparently no record of this congress has been retained. Due to the war, no congress was held until 14 years later.

6. The Sixth Congress (1952)

In reviewing the special features facing accountants gathered for this congress, Sir Harold Howitt, president of the congress, emphasized the following points:

> First, although all countries represented here today have, in varying degrees, suffered from changes in the value of money, we have not yet reached agreement as to how this problem is best dealt with in periodical accounting statements.
>
> Secondly, although taxation is no new subject, it is today so heavy in most countries that the state is, in effect, the major partner in the enterprise, and it is probably true to say that without the help of the professional accountant and the trust imposed in him, the state revenues could not be raised, and Government, therefore, could not function.
>
> Thirdly, the difficulty of raising or retaining capital for development or even for existence is materially enhanced by these two factors.
>
> Fourthly, whereas the accountant in public practice has to direct his thoughts and certainly his certificates primarily

to the past and to the present, the professional accountant who has entered the commercial field, and indeed the practicing accountant who helps him therein, thinks even more of the future. [38:8].

The selection of papers for this congress had been made with these special features in mind. They included papers on fluctuating price levels in relation to accounts, on accounting requirements for issues of capital, on the accountant in industry, on the accountant in public service, and on the incidence of taxation. This congress was notable for its attention to educational and professional movements in all of continental Europe, India, Australia, Canada, and the United States. [38:8].

7. <u>The Seventh Congress (1957)</u>

Jacob Kraayauhof, the president of the Netherlands Institute of Accountants, presided over this congress. Once again, the facilities were available to follow the proceedings in English, French and German. Papers were presented on principles of the accounting profession, budgeting, verification of the public accountant, the internal auditor, and on ascertainment of profit in business. Concerning professional standards, it was concluded that:

> Race, nationality and place of residence are not the factors which determine the suitability of the accountant for his task; any failure to recognize this will hurt the profession as a whole and the country where the failure occurs. The real determinant of the success or otherwise of the profession in any country is whether its members have the right character and ideals, the requisite training, ability and experience, a firm grasp of accounting principles, a sincere desire to serve their clients and the honesty and independence of mind without which the highest service to their clients cannot be given. [38:9].

The role of international congresses and conferences in achieving international uniformity of these standards is well stated in the proceedings as follows:

> The profession in every country has much to learn from the experience of others. International congresses and conferences not confined to one nation or institute are of the greatest benefit not only to those who attend but also to those who afterwards hear about them. The availability of accountancy literature and of a forum for discussion of opinions and ideas is also very important. [38:9].

In his closing remarks, Kraayauhof placed the responsibility for uniformity of auditing standards and accounting principles, but especially the former, upon the public accountant's shoulders. [38:9].

8. The Eighth Congress (1962)

This congress was presided over by Arthur B. Foye, the president of the AICPA. The sessions centered around the theme, "Auditing and Financial Reporting in the World Economy." The papers covered three basic subjects: accounting, auditing and financial reporting. Most of the papers presented on these three major subjects urged that steps be taken to hasten the further development, understanding and acceptance of standards of accounting, auditing and reporting on an international scale. All of the speakers recognized that the key to progress is organized research by the profession, both at the national and international levels.

According to Paul Grady, then chairman of the Accounting Principles Board of the AICPA:

> If we are in agreement on these premises, it would be difficult to see how there can be disagreement on the necessity for international standards of auditing, accounting and reporting as a means of improving the mutual confidence in

> business relationships which is our particular responsibility. It has been the consensus of the discussion meetings that agreement on auditing standards should not be a very difficult undertaking since it is entirely a professional matter. In the case of accounting and reporting standards considerably greater difficulties are presented and it will be necessary, through our research efforts, to reach a clearer status nationally as a condition precedent to the development of international standards. [38:10].

Grady urged the delegations to work to develop clearcut statements of their own national auditing, accounting and reporting standards. He hoped that, out of this foundation material, the accounting profession, on an international basis, would promote the highest and soundest of these standards wherever they may exist. [38:10].

9. The Ninth Congress (1967)

F. M. Richard, President of La Ordre des Experts Comptables, presided over this congress. The meetings were carried out in English, French, or German with simultaneous translation facilities available in all three languages. Among the goals of the congress stated by Richard was an emphasis on the pursuit of harmonization to meet the needs of multinational trade.

In welcoming the congress to Paris on behalf of the French government, M. Michel Debre, then Minister of Economy and Finance, said:

> The new horizons are not limited by state frontiers or the boundaries of national companies. You have already emphasized during your previous congresses--and this one will be the same--the problems of harmonization not only of principles but also of methods. This is, indeed, an essential element of progress which we must achieve, and which cannot be achieved except insofar as you yourselves, through your efforts in each of your countries and by your coordinated efforts on the international level, will allow the establishment in essential accounting problems of a common language . . . [38:10].

The "New Horizons of Accounting" was chosen as the theme of the congress. These horizons were analyzed in terms of the economic approach, the geographic approach, and the scientific approach. The geographic approach covered the pursuit of harmonization within the accounting profession all over the free world. The single most important reason cited for this need is the growth of multinational trade and investment, and calls for a common method of reporting. The speakers called upon the profession to (a) develop an international glossary, (b) establish comparable levels of qualifications in all countries, and (c) come up with a worldwide understanding of professional standards. Subjects discussed in this area were harmonization of accounting principles, international harmonization of auditing standards and procedures, accounting problems peculiar to international enterprises, and international investments.

Richard, president of this congress, called for international harmonization of accounting principles, auditing standards and reporting practices when he said:

> The development of international exchanges, the drive forward of multinational companies, the interpretation of financial markets make more necessary than ever some harmonization of the languages and principles of accounting and auditing. As in other spheres, this harmonization will be necessarily cautious and progressive. If this work of harmonization is not undertaken by the accounting profession, governments will one day take the initiative. [38:11].

Hence, there was at this congress, as at the previous congresses, especially the Seventh and Eighth, every indication of a strong desire for international understanding and cooperation and, more importantly, a call for harmonization.

10. The Tenth Congress (1972)

This congress was presided over by Sir Ronald Irish in Sydney, Australia. Its theme was "Financial Measurement and Communication." The official language was English with simultaneous interpretation into French, German, Japanese and Spanish. [38:11]. This was the first congress to be held south of the equator. Although the congress in Paris in 1967 stressed the need for international cooperation and the importance of the accounting profession adjusting to the needs of the international community, the Tenth Congress exhibited a stronger note of urgency concerning the development of a world organization to address international problems relating to world trade, as well as a strong desire to strengthen cooperation among the various accounting bodies. Prompted by this sense of urgency and cooperation, the heads of the delegations of the sixty countries attending the congress in Sydney unanimously approved the adoption of the International Working Party's Final Report. This led to the creation of the International Coordination Committee for the Accountancy Profession (ICCAP). [37:38].

Of these international congresses, Dr. Khalid Amin Abdullah of the Accounting University of Amman, Jordan, draws these conclusions:

> These congresses provide the opportunity to learn at first hand what is taking place in other parts of the free world and to participate in a broader exchange of information to the benefit not only of the profession at large but also to the economies of the participating countries. Practitioners should recognize the fact that our generation, and even more the generations to come, are entering upon a new

type of civilization. This civilization is technical and it is universal. It is of paramount importance to recognize this fact in order to equip our profession with international accounting principles, auditing standards, and financial reporting practices to cope with the new type of civilization upon which we are entering and meet its demands. The demands of international investors and traders for reliable reporting can be met only by an international profession with international principles and standards.

These International Congresses of Accountants have so far allowed accountants from many nations to get together and exchange thoughts, ideas, and experiences. However, with proper sponsorship and dedication, the future congresses will prove as useful descendants of the First, which resulted in the unity of the various accounting societies in the United States into one federation. [38:13].

E. THE INTERNATIONAL COORDINATION COMMITTEE FOR THE ACCOUNTING PROFESSION (ICCAP)

1. Its Structure

While the ICCAP delegates, all of whom are accountants, have a common purpose, the internationalization of the accountancy profession, there are barriers which must be overcome, including those of language and customs. But from the beginning meetings have been held in a spirit of considerable harmony and understanding. [37:38].

ICCAP has eleven members representing Australia, Canada, Federal Republic of Germany, France, India, Japan, Mexico, The Netherlands, Philippines, United Kingdom, and the United States. Each country appoints one delegate who represents the total accounting profession in his particular country. He is accompanied to meetings by a representative of the permanent staff of one of the accounting professional bodies in that country. This procedure has been adopted to ensure continuity in the work of the ICCAP. [39:146]. It is anticipated that delegates will be rotated over a period of years. [37:38].

The first Chairman of ICCAP is Dr. R. Goerdeler, the delegate for the Federal Republic of Germany. Germany will act as host of the Eleventh International Congress of Accountants, to be held in October 1977. [40:81].

In addition to periodic plenary sessions, working parties have been formed on special subjects, and considerable work is reported to have been done in developing the objectives and the approach that appear best suited to permit the ICCAP to accomplish its tasks. [40:82].

2. Its Objectives

The objectives of the ICCAP, as adopted at a plenary meeting in Mexico City in 1973, were defined as follows:

> The long term objective of ICCAP as established at the Tenth International Accountants Congress in Sydney, 1972 should be the development of a coordinated worldwide accounting profession with uniform standards. ICCAP should accept responsibility to give leadership towards the achievement of this objective and should take the following action:
>
> 1. Initiate, coordinate and guide work that has as its goal the achievement of international technical, ethical and educational guidelines for the accounting profession and reciprocal recognition of qualifications and work towards this purpose by establishing appropriate committees as well as working through the regional organizations for implementation.
>
> 2. Encourage and promote the development of regional organizations with common objectives and formulate guidelines for the structure and constitution of such regional organizations.
>
> 3. Review ICCAP's role, functioning and constitution and propose changes necessary to achieve its objectives. [39:146].

The most important factor is a firm decision by this body of eleven members to accept leadership for the development of a coordinated worldwide accounting profession with common standards. Achievement of this objective will not be easy.

3. Its Organization

To implement its objectives, ICCAP formed five standing committees in Mexico in 1973. These committees and their purposes are as follows:

a. Regional Bodies Committee

To consider the regions in which regional organizations should be encouraged and the practical steps to be taken. Also, to formulate the objectives, guidelines, and activities which should be suggested to these organizations. [40:82].

b. Ethics Committee

To develop national bodies with common standards and to formulate guidelines for the ethical principles to be adopted by these bodies in framing their ethical rules. [40:82]. To consider and recommend a model code of ethics for the profession internationally, and also to assist and advise professional bodies in drafting ethical codes. [40:82, 39:39, 37:149].

c. Professional Education and Training Committee

To formulate minimum standards of professional education and training to be adopted by professional accounting bodies, including the intellectual level of professional examinations as a condition for membership. [40:82, 39:39, 37:149].

d. Future International Organization Committee

To consider and to make recommendations to ICCAP on the constitution membership, financing, structure, and functions of an international organization of accounting bodies incorporating the agreed objectives of ICCAP. To submit these

recommendations for consideration by the Eleventh International Congress of Accountants at Munich in 1977. [40:82, 39:39, 37:149].

e. Publicity Committee

To ensure that the objectives of ICCAP are understood internationally prior to 1977. [40:82, 39:40, 37:149].

4. A Permanent Secretariat--Desirable but Distant

A permanent secretariat to take over the administration of ICCAP is an ultimate but evidently distant objective of the Committee. [37:38]. The view has, however, been expressed that substantial progress can only take place through the formation of a full-time body, and that an international secretariat could provide the institutional structure for such a body.

> We have recognized that a permanent full-time board is needed for setting accounting standards in the United States. A full-time board is even more essential if we are ever to have worldwide standards, where laws and customs vary greatly and may need to be changed to accommodate a single standard. The enormity of this task may be such that we cannot expect real progress through any organization, but the point is that we can be assured of making no progress if we do not set up an international organization and try to harmonize standards. [6:21].

F. INTERNATIONAL ACCOUNTING STANDARDS COMMITTEE (IASC)--FORMATION

At the time of the International Congress of Accountants in Sydney in 1972, the mood of the professional bodies seemed ripe to take positive steps forward toward the establishment of international accounting standards. In Sydney the United Kingdom proposed that an international committee should be set up in order to formulate international accounting standards. The response was immediate and positive. On 29 June 1973, the

International Accounting Standards Committee (IASC), with a full-fledged constitution of its own [42], came into existence. Its first chairman was Sir Henry Benson, a former President of the Institute of Chartered Accountants in England and Wales. The Committee consists of nine founder members comprising representatives of the accountancy professions of Australia, Canada, France, Germany, Japan, Mexico, The Netherlands, United Kingdom and Ireland, and the United States of America. [41:24]. The countries attending the congress at Sydney were invited to become associate members of IASC. [40:82]. The IASC is technically a part of ICCAP with autonomy for promulgating international accounting standards. It is apparent that, if ICCAP is to achieve its objective of the development of a coordinated worldwide accounting profession with uniform standards, the work of IASC is of particular importance.

The IASC issued its first definitive standard on the Disclosure of Accounting Policies in January 1975. [11, 41:27]. Table VI lists the program of work which IASC has set for itself. Sir Henry Benson has estimated that a minimum of 24 months is required to undertake the necessary research work, to prepare and obtain the approval of the Committee for an Exposure Draft, to circulate the Exposure Draft worldwide, and then to assess the comments received and finally formulate the definitive standard. [41:27].

TABLE VI

IASC Program of Work

Subject	Expected Date of Publication		Steering Committee Members
	Exposure Draft	Definitive Standard	
Inventories in the Context of the Historical Cost System	July 1974	July 1975	Canada, Japan, Mexico
Consolidated Financial Statements	Nov. 1974	Oct. 1975	Australia, Germany, USA
Depreciation	Apr. 1975	Apr. 1976	Australia, Canada, France
Information to be Disclosed in Financial Statements	Apr. 1975	Apr. 1976	Germany, Mexico, U.K., Ireland
Translation of Foreign Accounts	July 1975	Oct. 1976	Japan, USA, Netherlands
Inflation Accounting	Oct. 1975	Oct. 1976	Canada, Israel, U.K., Netherlands, Ireland
Sources and Application of Funds	Jan. 1976	Jan. 1977	Australia, France, South Africa
Presentation of the Income Statement including Extraordinary Items, Prior Period Adjustments, and Accounting Changes	Apr. 1976	Apr. 1977	Germany, Japan, USA
Research and Development	July 1976	July 1977	Canada, Mexico, New Zealand

Note: *The Wall Street Journal* of October 9, 1975 (p. 34) has announced the recent promulgation of the first of the standards listed above, dealing with inventory valuation.

Source: Ref. 41:29.

It is evident from Table VI that the subjects have been carefully chosen so as to go to the root of most published statements. If all these subjects are launched successfully in the next three or four years, IASC will have made a major worldwide impact on the form and content of financial statements.

If the initial enthusiasm with which IASC was started is continued, its impact in the years to come is likely to be important. Financial statements issued in every important nation of the world will comply with the standards promulgated by IASC or will disclose the extent to which there has been non-compliance. This is likely to improve the presentation of financial statements to the public, because more information essential to an understanding of the accounts will be made available. Moreover, there will be an increasing harmony in the accounting standards adopted worldwide, and comparisons will be facilitated.

VI. UNIFORM INTERNATIONAL ACCOUNTING--PROS AND CONS

Arguments for and against the development of international uniformity in accounting have tended to become polarized into two extreme viewpoints. Some arguments for uniformity seem to be tempered with a high degree of idealism, while some arguments against the idea tend to point out that such a plan would be unrealistic. In spite of these extremes, there are many accountants who hold the position that, although complete uniformity is impractical, some positive action toward international uniformity is needed. [43:31].

In carrying out a critical appraisal of these arguments with a view to assessing the general trend of thought in this area, it is necessary to recognize a very significant factor in the nature of these arguments. It will be observed that all of the arguments in favor of international uniformity in accounting deal with the desirability of the idea. The arguments against uniformity, on the other hand, do not attack the concept itself but rather question the feasibility of implementing uniformity. With the exception of the discussion of the problems pertaining to underdeveloped countries, the arguments against uniformity in no instance challenge the desirability of international uniformity. To this extent, it may be said that the arguments of the various writers concerned suffer from a common conceptual weakness in failing to make a case against the idea itself. However, this is not to imply

that arguments questioning the feasibility of uniformity are irrelevant or do not warrant consideration, any more than the arguments for uniformity are necessarily convincing in every case. On the contrary, as the last section of this chapter attempts to illustrate, while some of the writers both for and against uniformity have produced arguments that merit serious consideration, others appear to be merely speculative.

A. THE CASE FOR UNIFORMITY

1. Comparability

Probably the most frequently advanced argument in support of uniformity is the need for greater comparability of financial data in view of the rapid internationalization of business activities throughout the world today. This fact has been stressed in much of the literature concerning uniform international accounting and has been forcefully expressed by Professor Irving L. Fantl in these terms:

> With the expansion of business interests into every corner of the world, accounting is fast assuming global proportions. No longer can differences in reporting practices among nations be shrugged off as local problems to be dealt with by each community separately. The difficulties entailed become evident when the accountant of one country attempts to analyze a report prepared by an accountant of another country which employs different accounting procedures and auditing standards. In their desire to resolve this situation many accountants strongly advocate the establishment of an internationally uniform system of accounts and a standardization of accounting procedures. [5:13].

Especially from the viewpoint of the multinational company, worldwide accounting standards are needed to ensure that the results of each of its segments will be reported on a basis comparable to that used by all of its other segments.

Such comparable reporting is necessary for both internal and external financial reporting. For internal reporting, it is necessary to facilitate the adequate control of operations, decision making, and evaluation of performances of managers of segments. Comparable reporting by all segments of a multinational company is also necessary to enable top management to prepare consolidated financial statements for shareholders, creditors, and the public. At present, however, this is next to impossible because, as Adolf Enthoven writes:

> Unfortunately, the principles and rules governing international accounting practices are so varied and based on such numerous and contradictory theories that it is difficult to interpret them on an international or even a national basis. It becomes extremely hard . . . to compare and assess reliably financial statements . . .[13:117].

Therefore, common high professional accounting and auditing standards are needed so that investors will be able to place the same reliance on financial statements, regardless of the country of origin. Investors of all countries need some form of comparable financial information in order to purchase securities of corporations in different countries. At a time when foreign securities worth billions of dollars are listed on the New York Stock Exchange and American corporations are listed on major stock exchanges around the world, it is essential for investors to be able to make comparisons between firms in different countries. This can only be facilitated by increased comparability of financial statements of all companies, regardless of the countries in which they are domiciled. Such comparability would also contribute to more beneficial use of available capital. [44:34].

2. Credibility

Financial credibility is another powerful reason favoring uniformity in international accounting. From some of the remarks made in Chapter IV regarding the disclosure practices allowed or tolerated in a number of countries, it will be appreciated that greater mandatory disclosure by the firms of those countries is likely to improve their financial credibility. Private capital cannot flow freely over international boundaries unless investors can be furnished with reliable information about what is being done with their money. This can be achieved only if financial statements are audited according to a worldwide uniform set of standards by accountants in whom the investors have confidence. The latter requirement can only be satisfied by the existence of accounting professions in all countries having common levels of ethics and competency, based on uniformly accepted principles. [45:54].

The problem of credibility is especially pertinent to public capital, that is, government-to-government loans and investments. Specifically, these consist mainly of economic and military aid to the developing countries of Asia and Africa. In the case of military aid, since most of it is in the form of hardware, technical advice, and training assistance, the recipient countries are not greatly involved in accounting for the aid funds. But economic aid is usually extended by placing funds at the disposal of the recipient country. Most of the economic aid projects are implemented through the award of contracts by the recipient government to local or foreign firms.

Sometimes they are awarded to a consortium of firms from a number of countries. As the work proceeds, these firms render cost accounts to the government in accordance with their respective countries' accounting principles and practices. Thus, the accounting for aid funds, even within a single recipient country, may be done according to a variety of accounting principles and practices, depending on the countries to whose firms contracts for aid projects have been awarded. With a maze of accounting principles and practices from different countries to cope with, the donor country is severely restricted in its ability to maintain control over the utilization of funds committed by it for aid projects. It is not surprising that, in such a situation, opportunities for misappropriation of aid funds for unauthorized purposes are increased.

Effective control by donor countries of the utilization of aid funds by recipient countries could most efficiently be exercised through the medium of a common system of financial communication. Since there now exists a vast network of donor and recipient countries, and firms from many countries which contract to undertake aid projects, this amounts to the desirability or even the necessity of a uniform system of financial communication on an international basis. But the fact is that accountants continue to prepare financial statements in accordance with the practices of their respective countries, and in many recipient countries those practices are based on inadequately developed principles. As Donald T. Spindel writes:

> If financial statements are to be used by investors in other countries, certain basic financial information must be disclosed. Most foreign companies tell the public, including their own shareholders, as little as possible. For instance, in Germany, only dividends are reported. Reserve accounts conceal the rest of the income (if any). French companies were not required to report sales until 1961. As can easily be seen, international uniform accounting should improve disclosure of financial information by foreign firms. [43:32].

Uniform international accounting, therefore, appears to be the only method by which the credibility can be improved in the countries cited by Mr. Spindel and, indeed, in all countries.

3. Improved Communications

Another argument for the adoption of uniform accounting practices in all countries is that there is no other way of improving financial communications. Mueller has called accounting the "international language of business" [2:121], but this is not yet altogether true. As long as capital markets were national in scope, the need for financial communications between countries was not a matter of great importance. Consequently, the differences in accounting practices between countries was also not a serious problem. Now that the capital market is progressively becoming a single, worldwide market and companies are increasingly raising capital in countries other than those in which they are domiciled, more efficient financial communication is necessary; and this can only be achieved through worldwide accounting standards. However, until this becomes a reality, "the communication function that financial statements are meant to perform is severely inhibited by different accounting practices in various parts of the world." [44:29]. As discussed in an earlier chapter, differences in terminology

lead to misunderstanding and confusion. Spindel contends that much difficulty results when using a report written in a foreign language, or a translated report, and in trying to be familiar with every foreign accounting convention. [43:32]. The growth in the international character of business has been accelerated by the huge investments in underdeveloped countries, and this trend further supports the desirability of improved international financial communications. Financial statements prepared according to the local concepts of these countries fail to convey the right message to investors from other countries. Whether we are considering the question of investment in underdeveloped countries or between developed countries, the fact remains that, by setting uniform standards for international accounting, financial communications through the "international language of business" will improve significantly.

4. Improved Rate of Development

An interesting viewpoint put forward by some accountants is that through uniformity the pace of accounting development will be quickened to an extent which would not be possible under any other circumstances. [43:32]. They contend that 'uniform accounting will mean more scientific accounting,' [43:32] which they feel is highly desirable when today's society generally relies more and more on the application of the scientific method. According to them, the existing non-uniformity is the reason for a relatively slow rate of development of the state of the art. 'As the scientific method grows,' they say, 'accounting can no longer tolerate its

relatively slow pace of initiating changes.' [43:32]. Those who have adopted this line of thinking contend that 'scientific accounting,' which they equate with accounting uniformity, will quicken the pace of new accounting developments. [2:88-89]. Spindel elaborates on this concept when he says:

> Closely related to the scientific aspects of uniformity in accounting is that of a more unified and rational development of accounting theory. Apart from British, American, Canadian and Western European countries, few high standards or consistent practices exist. If accounting methods and procedures are established by using a uniform scheme, accounting development could be directed more exclusively to theoretical matters. Minimum attention would have to be given to accounting methods and procedures so that the development of accounting theory could proceed more rationally. Confusion over what is theory, what are methods and procedures, would be reduced. Greater international principles and practices could provide for even more unified theory advances. [43:33].

5. Training and Education

Another argument put forward in favor of uniformity is the attainment of better technical preparation and greater application of skills through a more coordinated training and education program. The accounting curriculum would be based on a scheme of international uniformity, and the education process resulting from this would improve professional standards. [2:110]. As to how undergraduate level international accounting courses ought to be managed, Norlin G. Rueschhoff has pointed out that international accounting covers all areas of accounting --managerial accounting, financial accounting, accounting theory, auditing and taxes. He contends that, if these areas are to be covered from a multinational perspective, determining the content of the undergraduate course should give extensive coverage to (1) financial accounting for international operations, (2)

multinational managerial accounting and control, (3) comparative international accounting principles, and (4) international financial reporting. [46:834]. Clearly, a syllabus based on Rueschhoff's recommendation, adopted worldwide in an internationally uniform setting, might enhance professional standards by encouraging academic competition through a uniform professional examination system on an international basis.

6. Economic Analysis

Gerhard Mueller has expressed the view that the adoption of uniform accounting would facilitate economic analysis by more accurate and consistent reporting of international macroeconomic statistics. [2:110-111].

7. The Underdeveloped Countries

The case of the underdeveloped countries is interesting because the problems of these countries have been used to produce arguments in support of both sides of the question. In support of the case for uniformity, C. P. Risardo Mora Montes, writing in The Canadian Chartered Accountant [47:40-41], begins by pointing out that the benefit of accounting, which in many developing countries does not exist or is incomplete, is indispensable for achieving economic development. Non-comprehension of financial responsibility and accounting concepts impedes economic progress, and developing countries are seriously handicapped in their efforts to develop economically because of the shortcomings in their accounting practices. Montes states that this is a matter of special concern to representatives of international financial and banking institutions,

which stress the need for improving the accounting and professional standards of underdeveloped countries in order to ensure the efficient use of financial resources. Montes believes that, although much is being done with financial aid programs, the transfer of accounting practices has lagged behind because the donor countries, lacking accounting uniformity among themselves, have been unable to assist the developing countries in developing accounting practices which would be equally acceptable to all the donors. In his opinion the accounting profession, recognizing that its contribution toward the economic development of developing countries must be made through the introduction of principles of accounting, standards of auditing, and methods of providing financial information to those countries, must devise such principles, standards and methods as are internationally acceptable.

In considering the reasons against international accounting the other side of Montes' contention will be presented.

B. THE CASE AGAINST UNIFORMITY

1. Inflexibility

Perhaps the most forceful argument against a scheme of international uniformity is the fact that the accounting concepts of individual countries are difficult to change. This is a hard reality. This viewpoint has been succinctly expressed by Spindel in these words:

> Accounting principles of one country have never been sold to another country. No matter how eager an accountant is to minimize differences, he may not be willing to accept the idea that some foreigner's accounting is better than

his own. This problem involves changing nationalistic attitudes and customs that may prove to be insurmountable hurdles. [43:33].

The problems of nationalistic and cultural differences have been elaborated in the first chapter. Even if these problems can be set aside and an attempt made to find possible areas of agreement for worldwide accounting standards, the extent of nonuniformity among nations, as emphasized in the third chapter, would probably render such an attempt very frustrating. Wilkinson points out that, even if an international plan of uniformity is accepted, attempts to cover the endless variety of circumstances that would arise in the real world would be an exercise in futility. In other words, no plan of uniformity could be so well devised as to take into account all possible contingencies. [44:30].

2. Limited Involvement with International Financial Statements

The Canadian Chartered Accountant expressed the opinion through an editorial [48] that, if private enterprises need a foreign firm's financial statements, they usually find an international accounting firm to prepare a report in accordance with their own local accounting standards. Due to this practice, few people are really concerned with international financial statements. This limited involvement leads to a general sense of indifference and what the editorial describes as "apathy" toward the idea of uniform international standards.

3. The Nature of Businesses

Wilkinson argues that the realities of business practices and the notion of uniformity are a contradiction in terms.

Businesses throughout the world vary so much that any attempt to treat their dissimilarities in a similar way would cause "distortions, overabundance of details, and meaningless disclosure". [44:34]. According to Wilkinson, even if uniformity could be attained under these conditions, it might be at a high price in the form of stagnation. Uniformity under these conditions may not be sufficiently flexible to adapt to changes in circumstances. It would not be able to respond to new ideas and new situations without upsetting the whole intricate balance of compromises between the systems of many countries. [44:35]. Mueller also reflects these views when he says:

> . . . a single set of accounting concepts and practices cannot possibly serve equally well in all the various accounting environments. Similarly, it cannot logically bridge the vast gulf between stages of economic development that range from the virtually undeveloped to the highly undustrialized. [2:235].

4. Expensive for Small Firms

Mueller cites excessive expense in small firms as a factor against the concept of uniformity. He says that even national uniform accounting plans have been costly for small enterprises and that, therefore, this problem is likely to be aggravated if international uniform accounting standards are established. He points out that, in Germany and France, the acceptance of uniform charts of accounts are generally limited to larger companies. [2:113].

5. Arbitration and Review

Another argument advanced by Mueller is that, for international standards to be effective, arbitration and review procedures would have to be established. This would involve a

governing body to enforce standards. In the absence of such an agreement, companies may be inclined to "window dress" their financial statements. [2:113]. Evidently, Mueller visualizes a very real problem in the creation of such a body.

6. Participation in Formulation

Spindel sees difficulties in the answer to the question as to which countries should take part in the formulation of a plan for uniform international accounting. He asks:

> Should only the United States, Britain, Canada, and Western Europe be included or should it also include underdeveloped countries? English-speaking countries? Capitalistic countries? [43:34].

And who decides what the answers to Spindel's questions are going to be? Perhaps the ICCAP, acting on behalf of the Tenth International Congress, has already done so.

7. The Underdeveloped Countries

Irving Fantl is the authority who cites the problem of the underdeveloped countries as an argument against the concept of international uniform accounting. Montes, whose viewpoint was presented in the first part of this chapter, cites this same problem as an argument in support of the concept. Fantl says that the establishment of uniform accounting standards has its full quota of champions in the less developed countries. These developing nations need capital, and the developed countries are the obvious source of that capital. The underdeveloped countries have a strong incentive to imitate the accounting practices of their donor countries, especially if, by doing so, they generate a confidence and stimulate the flow of capital. Such imitation is reinforced by academic

interchanges, whereby students from the recipient countries study in the institutions of the donor countries and learn their techniques. Both donors and recipients believe that the adoption of the former's practices will promote the development of the latter's economies. But Professor Fantl thinks otherwise. He says that the poorer countries function on a different economic basis, where private capital is virtually non-existent and the only entrepreneurs are the government and organizations such as Industrial Development Banks. According to Fantl, in a world of five-year plans, different financial criteria must be satisfied; and conventional evaluations lead to false conclusions when applied to economic planning. Fantl attributes the failure of most five-year plans of underdeveloped countries to the application of inappropriate evaluation techniques because "conventional methods of financial reporting are not satisfactory in an inflationary economy with a weak currency and no private capital." He urges the "accounting wisdom of advanced nations" to devise other methods of financial evaluation for these countries. He claims that the present blind conformity leads to "chaos rather than uniformity." Fantl's call to the advanced nations to "create a new system" to fit the peculiar circumstances of underdeveloped countries obviously negates the concept of uniform worldwide accounting practices. [5:13-16].

C. COMMENTARY ON THE ARGUMENTS

As stated at the commencement of this chapter, a significant difference between the general nature of the arguments for and the arguments against uniform international accounting exists in the literature. Except for Professor Fantl's arguments in relation to the problem of underdeveloped countries, it will have been observed that none of the arguments against the case for uniformity really challenge the concept itself. These arguments merely draw attention to the difficulties of implementation of the concept. Therefore, whatever the respective merits of the arguments of the various writers cited in this chapter, it may be stated that, while there exists an appreciable body of opinion in favor of the concept of uniform international accounting, the opposition to the concept is largely pragmatic rather than conceptual.

As regards the objections in the literature concerning feasibility, it may be appropriate to point out that progress, as understood by those directly involved, in any field of human endeavor would have been impossible over the years if feasibility alone had been allowed to be a stumbling block. This is perhaps true of the remarkable technological achievements of recent times. There is no reason to believe that it is any less true of progress in the accounting profession, as is apparently understood by an appreciable body of its members.

As regards the merits of the various arguments from the literature described in this chapter, a discussion of certain specific weaknesses in some of these arguments follows:

1. <u>Comparability and Beneficial Use of Available Capital</u>

Comparability of financial statements has been indicated as one of the most important benefits that would accrue from uniform international accounting. Among the arguments justifying the need for comparability, the literature points to the contribution which comparability would make to the optimal use of available capital. This contention is neither elaborated upon nor substantiated with illustrations. In view of the fact that an extensive literature on the theory of efficient capital markets has offered a number of sophisticated models to assist in the evaluation of the alternatives available on the capital market and these models invariably seem to rely on factors irrelevant to comparability, it is doubtful if comparability would be accepted by many experts as a significant consideration in making decisions relating to the optimal use of available capital. These models have been reviewed in Eugene Fama's article in <u>The Journal of Finance</u>, "Efficient Capital Markets: A Review of Theory and Empirical Work." [49:383-417]. From this review it becomes apparent that an evaluation of capital markets depends on factors such as statistically significant evidence derived from price changes, the extent of accessibility to 'information relevant for price formation' [49:414], (such as monopolistic access, publicly available access, etc.), derivation of "expected return" and numerous other considerations. A study of these models would reveal that an investor should, in deciding on resource allocation, look for and interpret various signals which are not dependent upon comparability.

2. Language and Translation Problems

In his discussion of improved communications as a reason favoring uniformity, Donald T. Spindel is of the opinion that international uniform accounting would remove difficulties arising as a result of using financial statements written in a foreign language or a translation thereof. The language problem is not peculiar to accounting alone nor, evidently, has it impeded efficient professional communications between nations in other skills. This is abundantly evidenced by productive technological cooperation between nations in a wide range of activities. In not substantiating his contention by being more specific, Spindel has failed to establish how the language problem would be solved by uniform international accounting. In fact, it may be argued that the non-comprehension of a foreign language is not necessarily a reason in itself for not being able to comprehend a foreign financial statement if a competent translation can be obtained.

3. 'Scientific' Accounting

The discussion contending that uniformity would promote the rate of development of accounting equates the phrase 'scientific' accounting with uniformity of accounting. This discussion does not elaborate on the term 'scientific' accounting and leaves its meaning unclear. The accounting profession endeavors to be very precise in the definition of terminology as one of its means of promoting high standards of accounting practices. The introduction of this undefined term naturally leads to hesitation in accepting it as a basis upon which any

argument can be constructed. In the absence of a precise definition of 'scientific' accounting, it would also not be possible to know whether uniform accounting is scientific. Moreover, the argument that states that uniform accounting would facilitate faster development may be countered by the argument that uniformity, by definition, would tend to reduce flexibility, which is often regarded as one of the prerequisites of development.

4. Variety of Circumstances

The inflexibility of uniformity has been used by Wilkinson as an argument against it. According to him, the variety of circumstances under which busineses operate in various parts of the world would render it difficult for a uniform system of accounting to be applied to all of them. Wilkinson does not support his point with anything more specific than a generalization and does not illustrate the kind of varying circumstances which might nullify the feasibility of uniformity. In fact, it may be argued that businesses within one country also vary considerably in their circumstances; but this has not prevented the implementation of uniform accounting practices within a country. The fact that two manufacturing firms, such as automobile assembly plants, are situated in two different countries does not necessarily suggest that their operations are so very different from each other that they have to adopt completely different sets of accounting principles and practices. In the absence of specifics, it is difficult to avoid the assumption that Wilkinson bases his contention on speculation.

5. Charts of Accounts

In objecting to the feasibility of uniformity on the grounds that it would be excessively expensive for small firms, Gerhard Mueller seems to visualize international uniformity as specifying a uniform chart of accounts. Such a requirement certainly would be very expensive for small firms. However, if the uniform accounting principles and practices in a large country like the United States can manage without this stringent requirement, there appears to be no reason to believe that common charts of accounts would be an indispensable necessity under international uniformity. Mueller's misgivings in this regard are unfounded because, as far as can be ascertained, this is not a requirement even within any individual nation's accounting practice; and there seems to be no reason why it should become one under international uniformity.

6. Underdeveloped Countries and Conventional Accounting Standards

Irving Fantl has asserted that the application of accounting standards of developed countries to the evaluation of economic planning and performance of underdeveloped countries is inappropriate. He claims that such inappropriate application leads to false conclusions and points to this factor as one of the causes of the frequent failure of five-year plans in those countries. Fantl, however, does not illustrate his point; and it is difficult to visualize a typical instance in which such a grave chain reaction is likely to occur. Fantl's contention is obviously of a very serious nature and would warrant

urgent consideration if he had substantiated it. But Fantl has not done so and the argument accordingly lacks depth.

VII. CONCLUSION--FUTURE PROSPECTS

Professor Gerhard Mueller, in his assessment of the future prospects of the feasibility of international uniformity in accounting, has written:

> International accounting uniformity is not a reasonable goal at the state of the art today--both conceptual and practical. . . The existence of basically different patterns of accounting development throughout the world, and the varying accounting concepts and practices these patterns have produced in their own individual environments, lead to the conclusion that a set of absolutely uniform international accounting standards is as unrealistic as an attempt to force the accounting concepts and practices of a single country upon all the rest of the world. . . Proper international standards in the accounting discipline as a whole ought to be comprehensive and general enough to require with them a recognition of different environmental influences upon accounting. [2:244].

Yet Professor Mueller, a leading authority in international accounting matters, seems to mellow his skepticism when he says:

> International corporations are in a unique position to innovate accounting and financial reporting practices that transcend national limitations. Free of nearly all precedents and shackles of long traditions, these corporations are in an ideal position to devise sets of accounting, auditing and reporting standards and practices that are particularly suited to their own special circumstances and are not bound by the social, political, legal or economic influences of any one country. International corporations should be able to lift their accounting problems above national ramifications and bring all underlying considerations into harmony with the real international character of their business operations. [2:222].

Whether or not Mueller's two statements above indicate a shift from the descriptive approach to the world accounting approach (or vice versa) discussed in Chapter II, the significant point here is the emphasis on the role of international

corporations in the development of international uniformity. From some of the available data it would seem that the accounts of international and multinational corporations represent the bulk of world business today. Writing in the Wall Street Journal, Charles N. Stabler says:

> The era of the multinational corporation, the so-called super-company, is upon us--to the point that a few hundred concerns have in recent years grown beyond the size of all but the wealthiest nations and currently dominate much of the world's production, resources and financial affairs. . . If a corporation's sales were to be equated with a nation's output of goods and services, then 51 of the world's 100 biggest money powers would be international corporations and only 49 would be countries. . . Large international companies currently do about $500 billion of annual business in each other's territories, or about one-sixth of the world's gross product; that's more than the entire gross national product of Japan. [33:1].

From these facts it is very evident that the future course of international accounting will depend largely on the accounting policies and practices which these giants adopt for themselves.

Given the growing internationalization of business, as represented by these international and multinational corporations, it would appear that forces are operating which are generating a need for development of international standards of accounting. It seems that the management as well as the shareholders of multinational corporations will demand a greater degree of international comparability of accounting standards and accounting measurements. Moreover, it is also likely that governments, trying to control the operations of multinational corporations, will become anxious to see that standards are applied consistently between one geographical area and another. Since international corporations, with help from the international

auditing firms, are in a unique position to observe, analyze, and deal with international problems of accounting, governments would be well advised to encourage these corporations to innovate. Governments would be making a mistake to bind them to traditional accounting concepts and practices that are prevalent in their own countries. "The very nature and outlook of these corporations is international," says Mueller. "Their accounting should be encouraged to become the same." [2:246].

The preceding suppositions of the interest of governments in international uniformity seem to be supported by facts and the statements of authorities well qualified to express an opinion on such matters. For example, Mr. J. P. Cummings, the representative of AICPA on the International Accounting Standards Committee (IASC), has rated "the prospects of viable international accounting standards in the near future" as extremely high. [34:55]. He cites the tremendous impetus and support of countries from all corners of the earth in the activities of the IASC. He points out that institutes from Belgium, India, Israel, New Zealand and Rhodesia have formally indicated their support of the IASC's activities by becoming associate members of it. The institutes of many other countries have also become or are becoming associate members to show their support for international standards, and support has also been shown for such standards by the Securities and Exchange Commission (SEC), and by the stock exchanges of New York, the United Kingdom and Australia. Bearing in mind the fact that the institutes of some countries may not be able to commit themselves to

activities of an international nature without the approval of their respective governments and also, of course, the support of agencies of government like the SEC, Cummings' remarks seem well founded. On the basis of these trends, Cummings is highly optimistic about the success of the present international accounting effort. [34:55].

For auditors in all countries where international standards are supported, and particularly in the United States, where so many multinational corporations are incorporated, the standards will greatly increase the comparability and meaningfulness of financial statements. Of course, ultimately the chief beneficiary will be the international investor and creditor who can confidently use and trust the financial statements prepared in any country.

Notwithstanding a world environment which seems to be favorable to the concept of worldwide uniformity in accounting, the fact remains, as mentioned at the beginning of Chapter VI, that many accountants doubt that uniformity is realistic. They are doubtful in the sense that they consider a truly worldwide set of accounting standards as unlikely and impractical. However, as also pointed out in Chapter VI, they recognize that it is unwise to advocate or tolerate the present situation; and they infer that the most likely solution to the problem would be one of compromise. As Wilkinson puts it:

> The harmonization must be approached without compromising the high standards existing in many developed areas and without attempting to select the practices of any one area and superimpose them on the world. [44:35].

These compromisers, however, have not been very specific in their proposals as to how their ideas ought to be implemented. In one instance where a plan was proposed it appeared rather airy and oversimplified. Robert F. Brandt came up with this three-phase plan [43:35]:

1. Identify the areas where fundamental differences exist and reduce or eliminate these differences.

2. Accept a course of action designed to develop an international codification of these principles and standards where feasible.

3. Implement a step-by-step procedure of the adopted plan.

Professor Brandt does not expand on this outline but the adoption of such a plan could be of great international benefit.

Probably a more realistic plan of implementation for the school of compromisers has been suggested by Irving Fantl. [5:16]. He points out that a misconception of international accounting is that the objectives of various systems are the same. Thus, the objective of each system must be defined. He suggests that the question, 'How well does the present accounting system fulfill its accounting objectives?' should first be ensured in any appraisal of a system. He cautions that the wholesale adoption of another country's system would be detrimental to the interests of accounting, and advocates the following action:

1. International accountants should develop a greater understanding of how economic systems interact in general and between individual countries and world areas.

2. Stronger links among accountants of all countries should be forged.

3. Practical solutions to diversity in worldwide accounting should be developed.

To further these ends, Fantl suggests the establishment of an international body of accountants, economists, government officials, educators, and others. These individuals should try to reconcile differences in accounting systems. Fantl visualizes the underlying quest for uniformity through the development of reconciliation systems as a reliable means to translate unfamiliar data into familiar terms. In essence, his idea of a compromise is 'a large superstructure of reconciliation systems.' [5:16].

Fantl considers that the success of such an exercise will surely contribute largely toward establishing worldwide confidence in financial statements and may facilitate the development of totally new capital markets, by which developing nations of the world can participate more fully in financing their own industrialization processes and thus help their economies to flourish. Fantl bases his proposals on the need for world accountants today to act in concert, to join together in programs that not only examine and reconcile their differences, 'but also explore the means of broadening world understanding of accounting and its critical role in progress.' [5:16].

In fact, Fantl's ideas do not vary materially from the present activities of the ICCAP and the IASC, discussed in Chapter V. His suggestion of a more broadly based body constituting members of other skills may be questioned by some accountants who feel that the accounting profession alone is qualified to deal with the challenge of international uniformity.

In this connection, William P. Hauworth, a partner of Arthur Andersen & Co., further emphasizes this point when he says that not even accountants are at present in a position to meet the challenge:

> Developing worldwide accounting standards that will apply to all companies and will be understood by all knowledgeable readers of financial statements is a more difficult task than developing standards for use by a single company. Such standards can be developed only by the accountants. However, at the present time the accounting profession as a body is not in a position to develop worldwide standards. No organization of accountants now existing has the authority to develop these standards, and no accounting organization or other body now functioning has the authority to enforce compliance with such standards. [9:33].

In other words, Hauworth considers that, if and when the climate is favorable for the development of enforceable international standards, only accountants will be competent to develop them. He evidently would not agree with this aspect of Fantl's suggestion. As regards his other remarks, the ultimate success or failure of the ICCAP's and the IASC's efforts would contradict or vindicate Hauworth's views. In the meanwhile, there can be no doubt that a proposal such as Fantl's, the intense interest in international uniformity being evoked by the International Congresses of Accountants, and the efforts of the ICCAP and IASC are likely to be representative of the general consensus of thinking of the accounting professions of all nations. This thinking is evidently one of cautious optimism that uniformity in international accounting will ultimately become a reality. This optimism, of course, implies that most accountants regard uniformity as a desirable goal.

Perhaps the accounting profession's outlook for the future of uniformity has been most appropriately expressed in the words of Gordon Cowperthwaite, Canada's delegate to ICCAP and Managing Partner of Peat, Marwick, Mitchell & Co.:

> We would be fooling ourselves if we believed that standardization of principles, practices, ethics and education can be achieved without major frustrations and disappointments. But in a world which is constantly shrinking in terms of the movement of population, currency, goods and services, an international profession must not be considered only as an ideal which we must work towards. It should be thought of as the next inevitable stage in the evolution of the accounting profession--otherwise we may lose the opportunity of fulfilling our function in tomorrow's society. [37:40].

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